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SAN FRANCISCO
PUBLIC UTILITIES COMMISSION



ANNUAL REPORT FISCAL YEAR 1997-1998



SAN FRANCISCO PUBLIC UTILITIES COMMISSION
1155 MARKET ST., 4TH FLOOR, SAN FRANCISCO, CA 94103 • TEL. (415) 554-3155 • FAX (415) 554-3161



December 1, 1998

Honorable Willie L. Brown, Jr., Mayor
Honorable Board of Supervisors

Dear Mayor Brown and Members of the Board:

In accordance with Section 4.103 of the Charter, I am pleased to forward the Annual Report for the Public Utilities Commission for Fiscal year 1997-98.

We were heartened that San Francisco voters approved in November 1997 Proposition A and B, authorizing \$304 million in bonds to maintain and upgrade The City's drinking water supply system.

City voters spoke again in June of 1998, passing Proposition H that called for the freezing of water and sewer rates until July 2006. We are working diligently to live within the confines of this proposition, while at the same time providing reliable water and wastewater services. It is important to note that before the passage of Proposition H, our Commission voted not to increase water and sewer rates for the third straight year.

In order to help offset operating costs and keep rates down, we made a concerted effort to improve non-rate payer revenues. \$6.2 million was generated in lease and permit revenues from SFPUC owned land and we successfully negotiated the sale of SFPUC property to BART for \$17 million. Aside from significant revenue for the City, this sale facilitated the BART extension to the San Francisco International Airport.

Additionally, in order to improve public health in the Bayview-Hunters Point District, the SFPUC worked closely with other City departments to persuade PG&E to shut down rather than sell its Hunters Point Power Plant.

Finally, more than \$45 million dollars generated by Hetch Hetchy through the sale of surplus hydro-power was transferred from the SFPUC to the City's General Fund and helped support important services such as healthcare and police and fire protection.

Sincerely,

Ann Moller Caen
President

DOCUMENTS DEPT.

MAY 11 2000

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SAN FRANCISCO PUBLIC UTILITIES COMMISSION MISSION

To serve San Francisco and its Bay Area customers with reliable, high quality and affordable water, while maximizing benefits from power operations and responsibly managing the resources entrusted to its care.

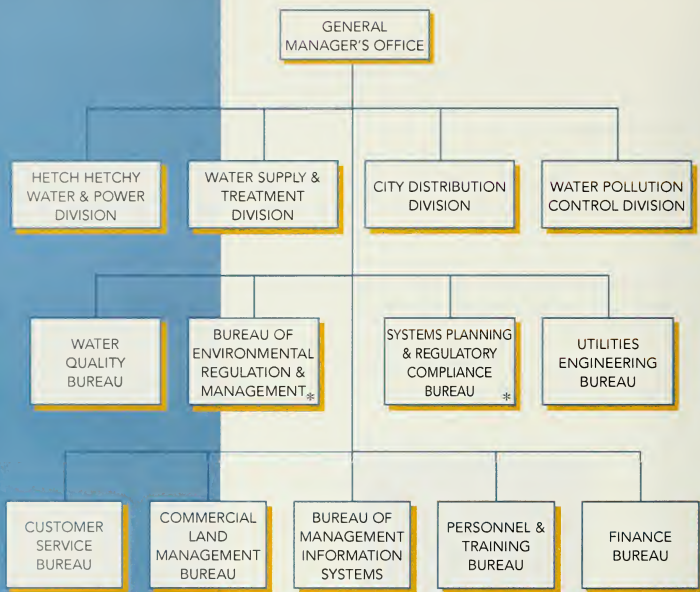
To protect public health and the aquatic environment by providing safe, reliable and efficient collection, treatment and disposal of San Francisco's wastewater.

To conduct its business affairs in a manner that promotes efficiency, minimizes waste and assures rate-payer confidence.

To promote diversity and the health, safety and professional development of its employees.



Public Utilities Commission



*NOW COMBINED

INTRODUCTION

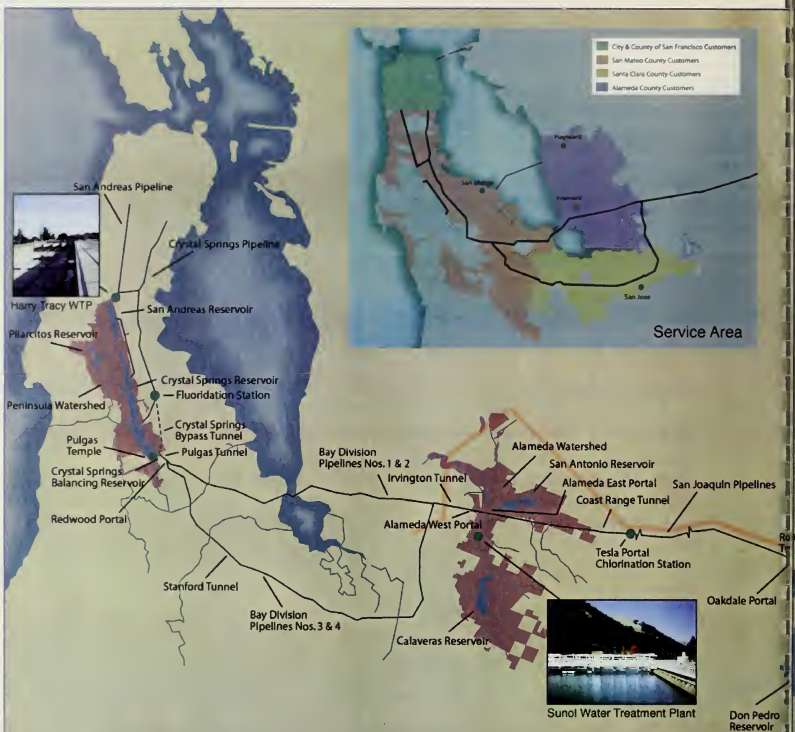
The San Francisco Public Utilities Commission (SFPUC) oversees three of the City's municipal utilities:

- 1 The Hetch Hetchy project, which consists of water supply and power generating facilities in the Sierra Nevada;
- 2 The water treatment and distribution system, which delivers some of the purest drinking water in California to more than 2.3 million customers in the Bay Area; and
- 3 The wastewater treatment and disposal system, which collects and treats sewage and storm water flows within San Francisco.

Each of the three utilities represents a separate enterprise within the SFPUC which operates as a department of the City and County of San Francisco. Services from the three utilities are provided to approximately three million people in six counties. The SFPUC comprises of 1,432 miles of water pipeline, 898 miles of sewer pipeline, and 244 miles of power pipelines. It has three water treatment plants, three wastewater treatment plants, 13 water reservoirs, and over 167,000 retail water customers and 30 wholesale customers. Its sewer plant capacity is 415 million gallons per day in wet weather. The SFPUC has eight electric power generation units with maximum kilowatt demand of 396,100.

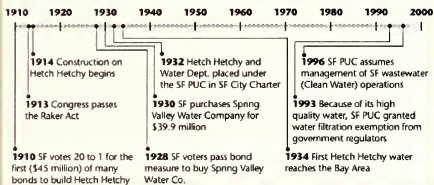
Four divisions are responsible for the operation of the utilities – the Hetch Hetchy Water and Power Division, the Water Supply and Treatment Division, the City Distribution Division, and the Water Pollution Control Division.

The SFPUC's utility system originates in the Sierra Nevada, where the *Hetch Hetchy Water and Power Division* maintains three reservoirs and more than 650 acres of watershed, much of which is located in Yosemite National Park. Water from the reservoirs is conveyed through a series of tunnels and pipelines from the mountains and across the Central Valley. En route, the water passes through four powerhouses, generating electricity for the City's municipal load and its other customers.



San Francisco Public Utilities Commission System Map

| 1910 | 1920 | 1930 | 1940 | 1950 | 1960 | 1970 | 1980 | 1990 | 2000 |
|------|------|------|------|------|------|------|------|------|------|
|------|------|------|------|------|------|------|------|------|------|



Holm Powerhouse



Moccasin Powerhouse



At Tesla Portal in the East Bay, the Hetch Hetchy water becomes the responsibility of the *Water Supply and Treatment Division*. The *Water Supply and Treatment Division* also draws another 15% of the total water supply from five reservoirs located in the East Bay and on the Peninsula. Water from these local sources is treated at two plants before it is delivered to City customers and 30 wholesale water surveyors in the San Francisco Bay Area.

At the City of San Francisco's border, the *City Distribution Division* assumes responsibility for storage and final delivery to San Francisco customers. The Division maintains eleven reservoirs and eight storage tanks within the City, and uses a series of pump stations and more than 1,200 miles of water mains to reach every elevation and corner of the City.

Finally, the City's wastewater discharge and storm water runoff are captured by more than 900 miles of sewers and storm drains. The *Water Pollution Control Division* maintains the wastewater collection system and operates three treatment plants, where chemical and biological treatment processes are used to remove pollutants before the wastewater is discharged into San Francisco Bay and the Pacific Ocean.

In addition to these four operating divisions, there are nine bureaus that provide technical and administrative support services. This approach eliminates duplication of effort and contributes to more efficient operations.



Secondary Clarifiers, Southeast Water Pollution Control Plant

The Commission

The SFPUC is led by five Commissioners, appointed by the Mayor who serve overlapping four-year terms. The Commission, in turn, elects one of its members to serve as its President each year. The Commission and the Mayor appoint the General Manager who serves as the chief administrative officer and is responsible for the SFPUC's day-to-day operations in accordance with the Commission's policies, the City Charter, and the Administrative Code. The General Manager appoints senior staff to run the three utilities.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION MEMBERS DURING FY 1997-98:

Victor G. Makras, President
Ann Moller Caen, Vice President
E. Dennis Normany
Robert K. Werbe
Frank L. Cook

HETCH HETCHY WATER AND POWER DIVISION

The Hetch Hetchy Water and Power Division is responsible for more than 85% of San Francisco's water supply and for the generation of electricity from that resource. Approximately one-third of the electricity is used by the City's municipal customers (e.g., the Municipal Railway, the Recreation and Parks Department, the Port, City hospitals, street lighting, the Moscone Center, and the water and sewer utilities). The balance of its power is sold to other publicly owned utilities, such as the Modesto and Turlock Irrigation Districts. The Hetch Hetchy Project consists of reservoirs, hydroelectric power plants, aqueducts, pipelines, and transmission lines. This system carries water and power more than 165 miles from the Sierra Nevada to customers in City of San Francisco and the portions of the surrounding Bay Area.

Hetch Hetchy operates as two related but separate water systems and associated power components. The primary system diverts domestic water from the Hetch Hetchy Reservoir to the Water Supply and Treatment Division through the Kirkwood and Moccasin Power Plants. The second system diverts water from Lake Lloyd and Lake Eleanor to the Don Pedro Reservoir through the Holm Power Plant. Water impounded in the Don Pedro Reservoir satisfies the Raker Act entitlements of the Modesto and Turlock Irrigation Districts, while allowing greater flexibility in domestic water use from the Hetch Hetchy Reservoir.

Electric power generated at four power plants is conveyed through approximately 165 miles of high voltage transmission lines to delivery points within the Modesto and Turlock Irrigation Districts, and an interconnection with Pacific Gas and Electric's ("PG&E") system for transmission to San Francisco for municipal purposes.

HIGHLIGHTS FOR 1997-1998

Water Year – Over the past 12 months, the Hetch Hetchy Reservoir received over 55 inches of precipitation, making this the third wettest year in the last recorded 80 years. Experts disagree as to whether El Nino was responsible; but in any event, the spring snow melt produced 906,000 acre feet of water which is about 150% of the historic average and 2.5 times the total capacity of the Hetch Hetchy Reservoir in just four months. At Lakes Lloyd and Eleanor,



Moccasin Powerhouse

the numbers were equally impressive at 180% of historic average spring runoff, or 560,830 acre feet of water over a four-month period. A steady snowmelt was also beneficial for power operations.

Electric Business Activities – The implementation of last year's agreement with PG&E resulted in increasing the City's municipal load by approximately 12%. In addition, Hetch Hetchy was integral to the successful completion of several important City projects, including expansion of maritime activities at the Port of San Francisco and completion of the new Children's Center at Yerba Buena Gardens.

Hetch Hetchy, working closely with staff at the San Francisco International Airport, completed the first of several new facilities to expand the Airport's electric service capacity. Also, in the last year, Hetch Hetchy has further developed its in-house capability to provide a broad array of energy services, including design consultations, construction, operations and maintenance of electric distribution facilities, and meet the significant challenges of the new restructured electric market. Through its Bureau of Energy Conservation ("BEC"), Hetch Hetchy is about to commence a major lighting retrofit of one million square feet at 13 City College facilities. In addition, BEC has completed design reviews for the several important City projects, including the new County Jail with a projected savings of \$2 million in energy costs over the first 15 years and a reduction of carbon dioxide emissions by nearly 40 million pounds.

Electric Utility Deregulation – Hetch Hetchy continues its active participation in state and federal regulatory proceedings where the future structure of the electric industry is being decided. Key among these activities was Hetch Hetchy's participation in the PG&E divestiture process before the California Public Utilities Commission where the fate of PG&E's Hunter's Point and Potrero Power Plants was decided. The combined efforts of the Mayor's Office, the Public Utilities Commission, Hetch Hetchy, and the local community resulted in a promise from PG&E to shut down the most polluting of these plants, the Hunters' Point Power Plant, as soon as a new replacement generation and/or transmission facility can be constructed. Projections are that this may be accomplished within four to five years. Hetch Hetchy continues to play an active role in other facets of the electric industry to protect the City and its residents and businesses.

Powerhouses/Maximum Capacity
(Megawatts)

| | |
|------------------|--------------|
| Holm | 165 MW |
| Kirkwood | 122 MW |
| Moccasin | 115 MW |
| Moccasin Lowhead | 3 MW |
| | <hr/> 405 MW |

Treasure Island is one of several military establishments in the Bay Area being closed under the federal Base Realignment and Closure Act. The SFPUC helped the transition from the U.S. Navy to local control through a \$2 million "Cooperative Agreement" under which the SFPUC provided operations, management, maintenance and repair of the Treasure Island/Yerba Buena Island water, sewer, storm water, electric and gas utilities systems. The agreement was renewed for an additional year, with an option to renew for two more years while the City and the Navy negotiate the transfer of the property to the City.

Hunter's Point Naval Shipyard – The SFPUC is similarly playing a active role in the City's plan to acquire this shipyard. The shipyard is an EPA Super Fund site and the utilities systems are in significant disrepair. The SFPUC is working closely with the Mayor's Office and the San Francisco Redevelopment Agency to assess and mitigate the financial and operating risks of this major development effort. It is anticipated that the City will take title to at least a portion of this closed military base on or about July 1999.

LOOKING FORWARD

In the coming year, Hetch Hetchy will ramp up its efforts to improve its business operations in order to survive the effects of the newly competitive and volatile electric market. Hetch Hetchy will continue to work towards securing the City's energy future through energy conservation and the development of clean, efficient renewable resources. Hetch Hetchy's Bureau of Energy Conservation (BEC) will initiate its first large-scale retrofit project in Fall 1998 at

General Hospital, and has secured grant funds from the California Energy Commission to subsidize development of two renewal projects: The Southeast Treatment Plant Digester Gas Project and the Calaveras Small Hydroelectric Project.

Hetch Hetchy will also continue to work closely with the local communities and the Mayor's Office to close the Hunters' Point Power Plant.



Bay Division Pipelines

WATER SUPPLY AND TREATMENT DIVISION

The Water Supply and Treatment Division assumes responsibility for water from Hetch Hetchy at the Tesla Portal in San Joaquin County. From there, the water is conveyed through four pipelines to customers located in Alameda, Santa Clara and San Mateo counties, as well as San Francisco. The Division provides another 15% of the total water supply from reservoirs located in the East Bay and on the Peninsula. These local water sources require filtration and treatment at two plants. In 1997-98, the Water Supply and Treatment Division delivered on average 250 million gallons per day (mgd) to customers throughout the service area.

HIGHLIGHTS FOR 1997-1998

The Division conducted a number of activities in three major areas in the course of the year. The most significant accomplishments are summarized below:

Land and Resource Management

- Completed the draft Watershed Management Plans, with the draft Environmental Impact Report underway.
- Completed mitigation measures associated with the Calaveras pipeline project.
- Started the Rights-of-Ways Management Planning effort under the direction of the Division's new Right-of-Ways Manager.
- Initiated biological studies and assessments in relation to the Bay Area Ridge Trail and the Alameda Fisheries Restoration Program.
- Using the Conservation Corps, accomplished fire hazard reduction work (vegetation management) in watershed lands.

Facility Improvements

- Placed in service a new reservoir, along with replacement of one supply well pump for the



Sunol Water Treatment Plant

Productivity Task Force

The Water Supply and Treatment Division has created a Productivity Task Force to identify areas where the division can increase the efficiency and effectiveness of the operation and maintenance of the water treatment facilities. The Task Force is investigating productivity improvements such as scheduling, cross-training, information management, preventive maintenance, and supervision.

- Castlewood service.
- Removed and replaced filter media in four filter beds at the Harry Tracy Water Treatment Plant.
- Increased liquid oxygen storage for ozone production by over 200% at the Harry Tracy Water Treatment Plant.
- Upgraded the chemical storage and feed system to enhance safety, reliability and process at the Harry Tracy Water Treatment Plant.
- Constructed and placed in operation a new chemical feed station for non-ionic polymer, for the purpose of enhanced coagulation at the Sunol Water Treatment Plant.
- Designed and installed new baffling in the waste wash water recovery ponds to improve the quality of wash water being recycled back into the plant at the Sunol Water Treatment Plant.
- Obtained the Phase III Partnership for Safe Drinking Water Award at the Sunol Valley Water Treatment Plant which was one of the first such plants to receive this award.

Operations Planning

- Efforts are now well underway in the development of a comprehensive preventive maintenance program to include all facilities and equipment within the division.
- In conjunction with the Bay Area Water Users Association, revisions and improvements are being made to the Emergency Operations and Notification Plan.

LOOKING FORWARD

In the coming year, the Water Supply and Treatment Division will continue the initiatives started in 1997- 1998 as well as several new efforts.

- A Division-level emergency response plan will be developed, and a response team will be designated and trained in the plan.
- A fire incident reporting and data collection process will be developed for Land Resources Management.
- Increased construction activities at the two treatment plants must be managed while maintaining water treatment and delivery capabilities.
- Phased implementation on recommendations made by the Productivity Task Force on scheduling, cross-training, information management, preventive maintenance and supervision.

Storage Capacity of In-City Reservoirs

(millions of gallons)

| | |
|-------------------------|-------|
| <i>Sunset</i> | 176.7 |
| <i>University Mound</i> | 140.9 |
| <i>Sutro</i> | 31.4 |
| <i>Summit</i> | 14.0 |
| <i>College Hill</i> | 13.5 |
| <i>Stanford Heights</i> | 12.9 |
| <i>Merced Manor</i> | 9.5 |
| <i>Lombard</i> | 2.7 |
| <i>Hunter's Point</i> | 1.1 |
| <i>Potrero Heights</i> | 1.0 |

- Maintains, repairs and upgrades as necessary 1,250 miles of water mains.
- Protects and coordinates work done by others to assure that San Francisco Water Department facilities are not damaged or destroyed.
- Installs, repairs and maintains services connecting individual customers to water mains.
- Identifies and repairs underground leaks.
- Performs landscape maintenance of 984 acres of Division land, including right-of-ways, reservoirs, open space and parks.

HIGHLIGHTS FROM 1997-1998

Water Main Repair and Replacement – As part of the continuous water main repair and replacement program, the Division replaced 30,700 linear feet of water mains.

The Division also made the following types of repairs:

| | |
|---------------------------------|-----|
| Main breaks | 105 |
| Connections | 88 |
| Main extensions and relocations | 8 |
| Steel main leaks | 3 |
| Cut in new gate services | 6 |

Service Renewals – Water services connect individual customers with the City's water mains. The Division is responsible for connecting new customers, maintaining and replacing deteriorated services and installing new meters:

| | |
|---------------------|-------|
| New services | 159 |
| Service renewals | 710 |
| Meter installations | 6,579 |
| Service Maintenance | 5,234 |

Meter Replacement – The Division has an ongoing program to monitor and replace the more than 167,000 meters that measure the amount of water delivered to each customer. Accurate meters help ensure that customers are billed properly for their water consumption. This year's meter replacement activities included:

| | | | |
|--------|-------|---------------|-------|
| Set | 739 | Scrap | 6,410 |
| Change | 6,971 | Special test | 788 |
| Repair | 350 | Field repairs | 2,938 |
| Home | 256 | Shop changes | 210 |

Treasure Island – In April 1997, the Navy contracted with the City to maintain and operate the water distribution system serving Treasure Island and Yerba Buena Island. The system, which consists of four reservoirs and four pump stations as well as water mains and connections, is old and in disrepair and lacks modern controls. The City Distribution Division is working with Treasure Island representatives to maintain the water system.

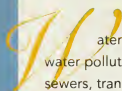
LOOKING FORWARD

The Division will work with the Utilities Engineering Bureau and Water Quality Bureau, intends to continue much needed repairs to reservoirs, pump stations, storage tanks and other facilities that are reaching or have exceeded their life expectancy.

WATER POLLUTION CONTROL DIVISION

Mandate for Water Pollution Control

In 1972, Congress passed the Clean Water Act, which set in motion a nationwide effort to clean up the nation's waterways. In response, San Francisco devised a "Master Plan for Wastewater Management" which would control overflows of untreated wastewater and upgrade the City's treatment plants. In 1997, after investing more than \$1.5 billion of federal, state, and local resources, the City is in compliance with all the requirements of its wastewater discharge permits.



Water Pollution Control operates and maintains the City's water pollution control system. The system is made up of collection sewers, transport and storage boxes, pump stations, overflow structures, treatment plants and outfalls. The Division's mandate is to maximize treatment and minimize combined sewage overflows, as dictated by the discharge permits issued by the state regulatory authority.

San Francisco has a combined sewer system in which both domestic and commercial/industrial sewage as well as storm water runoff are collected in the same sewer. As a result, the system captures and treats more wastewater to a higher level of treatment than nearly any other system in the greater Bay Area. During dry weather, the system collects, treats and discharges an average of 90 million gallons of sewage a day. When it rains, the system may collect and treat as much as 465 million gallons of combined sewage and storm water a day.

HIGHLIGHTS FROM 1997-1998



A schematic map of the wastewater system.

Water Pollution Control is responsible for maintaining more than 900 miles of sewers, operating 20 pumping stations and three wastewater treatment plants, identifying and implementing system repairs and improvements and planning for future operations. Significant achievements in 1997-98 were:

El Nino – With double normal rainfall, the Division facilities treated the most wastewater ever. The summer maintenance program, combined with excellent emergency response from the maintenance section,

allowed operations to maximize treatment throughout the entire rainy season.

North Point Plant Improvements – The second of several phases of improvements to the North Point Plant was initiated. These improvements will consolidate the treatment processes at the facility and improve the energy and operational efficiency of the plant.

Southeast Plant – Improvements to the Distributed Control System were completed. Currently, there is a two-year contract to repair the aging and corroding aeration process facility. An emergency contract was initiated to resolve a flooding problem in the area of Custer and Davidson Streets.

Oceanside Plant – The plant qualified for an Association of Metropolitan Sewerage Agencies (AMSA) Gold Award for excellent compliance with discharge permit conditions. In-house piping changes allowed the Division to begin co-thickening sludges. The resulting increase in cake solids and reduction of foam and scum means lower cost of hauling and avoidance of costly secondary system upgrades.

Treasure Island – The Division continued operation of the wastewater system on Treasure Island, which also serves Yerba Buena Island, on a contract basis with the Navy. In addition to operating the collection system, treatment plant, and 35 pump stations, the Division continues to assess requirements for future City ownership.

LOOKING FORWARD

In the coming year, the Division intends to place increased emphasis on the maintenance and repair of the sewer collection system. This effort will expand the cleaning program to reduce odors and backups and assure compliance with discharge permits. The Division is investigating options to continue permit compliant operation within the fiscal limits imposed by voter approved Proposition H which effectively froze the water and sewer rates at their current levels until July 1, 2006.

SFPUC BUREAUS

The four operating divisions receive technical and administrative support from nine service bureaus. This approach eliminates duplication of efforts and contributes to more efficient operations. Several functions have been reassigned among the bureaus to improve services to the operating divisions and, ultimately, to customers.

UTILITIES ENGINEERING

The Utilities Engineering Bureau provides engineering and construction management services for the water, power and clean water capital improvement programs of the SFPUC. The Bureau assesses the condition of storage, transmission and treatment facilities, and recommends necessary repairs or upgrades. It then designs the facility improvements to meet operating needs within budget and scheduled constraints. In 1997-98, the Bureau was responsible for \$100 million in capital improvements to water and power facilities.

HIGHLIGHTS FROM 1997-1998

- Design and construction of a replacement for the deteriorated Castlewood Reservoir in the East Bay, and installation of a new groundwater well, at a cost of \$2.2 million.
- Design of the \$2.5 million upgrades to chemical feed systems and facility improvements at Thomas Shaft which is the final disinfection point for water supplies to San Francisco and its wholesale customers.
- Design of the \$14.5 million underground bypass of Priest Reservoir in the Sierra Nevada mountains to protect the quality of San Francisco's Tuolumne River water supply from seasonal contamination due to debris from feeder streams or migratory birds.
- Preliminary engineering and design of \$8 million in seismic improvements and upgrades to the chemical feed, filtration and control systems at Sunol Valley Water Treatment Plant and seismic upgrades to San Antonio Pump Station which pumps water to the treatment plant.
- Initiation of the \$1.5 million restoration of the Sunol Water Temple, an architecturally significant landmark designed by



Willis Polk and built in 1910 at the confluence of the three original East Bay sources of San Francisco's water supply.

- Design and construction of \$14 million in emergency repairs to pipelines, watershed roads, electrical systems, power lines and water treatment facilities damaged from flooding and landslides from major winter storms.

FINANCE

The Bureau of Finance provides financial support and direction to divisions and bureaus of the SFPUC. The Bureau's functions include: Development, preparation, and monitoring of annual operating and capital budgets; preparation of monthly reports and annual financial statements; development of projections of water and sewer revenues; development and implementation of short and long term debt program; internal audits; and determination of wholesale and retail water and sewer rates.

HIGHLIGHTS FROM 1997-1998

- Completed full implementation of Clean Water financial information into the SFPUC.
- Developed a financial Policy and Procedure Manual that was distributed to operating units for reference.
- Completed ADPICS/Purchasing training throughout the SFPUC.
- Qualified \$304 million of water bonds for the ballot that were approved by the voters of San Francisco.
- Established a short-term debt Commercial Paper program. It is estimated that this program will save over \$1 million a year in interest costs.
- One of the first city departments to implement the new citywide integrated fixed asset system Fixed Assets Accounting and Control System (FAACS).
- Instrumental in the development of SFPUC standardized consultant contracts with defined rates for all miscellaneous fees, charges and overhead.



MANAGEMENT INFORMATION SYSTEMS

The Bureau of Management Information Systems (BMIS) provides data processing, computer systems development and office automation services to all SFPUC divisions and bureaus. The Bureau maintains and improves computer systems for processing water and sewer billing data, vehicle maintenance data, and payroll and other financial data. To support these and other functions, the Bureau operates a central computer center 24 hours a day, seven days a week. The Bureau also maintains a computer network of more than 500 microcomputers, which are installed throughout various SFPUC locations.

HIGHLIGHTS FROM 1997-1998

In 1997-1998 the Bureau made the following improvements in the SFPUC computerized systems:

- Implemented and deployed Intranet accesses to pertinent financial data to key managers throughout the SFPUC in support of more timely access to this data.
- Improved the internal efficiency of the BMIS mainframe operation with the installation of robotic tape units that require no operator intervention.
- Implemented Industrial Peer to Peer (IPP) access to real time plant status information at both filtration plants to provide remote monitoring of conditions.

PERSONNEL AND TRAINING

The Bureau of Personnel and Training provides services related to human resource and payroll management, and acts as the liaison with the Department of Human Resources, the Civil Service Commission, and the Controller's Payroll Services Division. The Bureau functions include: classification, examination, payroll position control, labor relations, disciplinary matters, affirmative action and equal opportunity compliance, training and general personnel administration. The 1997-1998 was a year of tremendous changes in Bureau staff as well as the staff of the entire SFPUC.

HIGHLIGHTS FROM 1997-1998

- Developed and delivered training in Diversity, Prevention of Sexual Harassment, EEO Principles, and restructured the New Employee Orientation thus reducing the length of orientation by 50%.

- Implemented the Municipal Executive Association (MEA) Pay for Performance, and updated and reissued a single reference manual for all Performance Appraisal Processes and Policies.
- Established new recruitment procedures for the Project Managers classification series.
- Classified 59 new positions.
- Administered 12 examinations.
- Completed the processing of 210 permanent and provisional employees.
- Participated in citywide labor negotiations with three unions.
- Implemented a Workplace Violence Management Response Program.

WATER QUALITY

The Water Quality Bureau (WQB) ensures that the SFPUC complies with all current and future water quality regulations, including the Federal Safe Drinking Water Act, the California Code of Regulations Title 22, San Francisco Ordinance 84-356 (Cross Connection Control), and sections of the Federal Clean Water Act. WQB assures compliance through water quality sampling and analysis, process engineering, applied research and data review, field inspections, cross connection control program management, field project oversight, regulatory liaison, hazardous materials management, and laboratory testing. The Bureau also responds to all customer complaints and inquiries and posts beach safety warnings after sewage overflows.



HIGHLIGHTS FROM 1997-1998

- Continued integration of the SFPUC Laboratory (Water and Clean Water Enterprises) and established new customer accounts, while providing for efficiencies and cost-savings among utilities. Attained certification for trace element analysis for drinking water and consolidated these analyses at one location.
- Collected over 111,000 drinking water and wastewater samples in the service area stretching from Yosemite National Park to the Pacific Ocean.
- Conducted over 600 analytical (i.e., chemical, microbiological, biological, and physical) tests on drinking water and wastewater samples.
- Developed internal Giardia and Cryptosporidium analytical capabilities.

- Processed 6,156 backflow prevention device tests and inspected 610 new backflow device installations to prevent contamination of drinking water with unsanitary sources. Initiated program to assess potential for contamination of the potable water distribution system from the Fire Department's high pressure Auxiliary Water Supply System.
- Completed 12 months of monitoring, required under the United States Environmental Protection Act ("USEPA") mandated Information Collection Rule ("ICR"), a nationwide data gathering project designed to assist in the formulation of new regulations related to microbiological contaminants and disinfection byproduct. Obtained a special testing waiver thereby saving \$100,000 in operating costs. Established a SFPUC web site for publication of ICR data.
- Received the Environmental Protection Act/American Water Works Association ("EPA/AWWA") Partnership for Safe Water Phase 3 Award (to improve water treatment plant operations, particularly Cryptosporidium removal, without significant capital expenditure) for the Sunol Valley Water Treatment Plant. Submitted the required water quality compliance report and application for the Harry Tracy Water Treatment Plant.
- Established satellite offices at Water Enterprise Divisions (i.e., Moccasin, CDD, Harry Tracy and Sunol Water Treatment Plants) to provide daily operation and technical support and improve response time to water quality incidents.
- Responded to more than 325 consumer complaints within four hours of initial contact.

CUSTOMER SERVICE

The Bureau initiated a Customer Service Improvement Task Force comprised of multi-disciplined volunteers from throughout the bureau; the Task Force generated a number of recommendations for improving services to customers, many of which have been and continue to be initiated.

The Customer Service Bureau is the primary point of contact with the SFPUC for water and sewer customers. The Bureau maintains 144,381 residential accounts and 22,944 commercial and municipal accounts in San Francisco. It provides for billing and collection of water and sewer charges, administration of customer accounts (including opening and closing accounts), installation of new services, meter reading, and field services such as inspections. The Bureau oversees the ultra-low flow toilet rebate and give-away programs and administers a water conservation "best management practices" program.

The Bureau is also responsible for the development of public information programs for water and sewer construction projects, and serves as an administrative source for water and sewer complaints.

Among its public information functions is the administration of a SFPUC speaker's bureau and the preparation of publications, such as the semi-annual *Water Quality Report* and billing inserts.

HIGHLIGHTS FROM 1997-1998

- Developed a "cafeteria plan" of payment options to provide payment convenience for SFPUC customers.
- Developed a Customer Service web site for new customer information and various conservation-related services.
- Initiated efforts to more cost effectively manage operations in such areas as collection, delinquency collection and mailing of customer bills.
- Developed a customer Bill of Rights that was sent to all customers in their bimonthly bills.
- Distributed 4,800 ultra-low flow flush toilets to the general public at six citywide sales events.
- Initiated the development of a business recovery plan that allows normal business operations to restart after a disaster.
- Sponsored an initial environmental internship program and a summit for high school students.
- Implemented training programs for managers and supervisors. Also, developed a program to improve customer relations' skills, which were conducted by a multi-discipline volunteer training group.



COMMERCIAL LAND MANAGEMENT

The Bureau of Commercial Land Management manages the SFPUC's commercial interest in lands and properties owned by the SFPUC. The Bureau monitors lease and permit negotiations, insurance renewals, delinquent rent collections, property taxes and assessments, and land sales and purchases. Its staff also recommends policies to the SFPUC and implements procedures approved by the SFPUC relating to land use, rental, management, and disposal of properties under its control. The Bureau seeks to identify means of increasing revenues by developing innovative uses of pipeline rights-of-way, treatment facilities, and watershed properties in a manner consistent with the goals of the SFPUC.

HIGHLIGHTS FROM 1997-1998

- Negotiated eight new leases.

- Issued 13 permits.
- Sold surplus lands totaling \$1.14 million in value.
- Collected \$6.26 million in lease and permit revenues.
- Negotiated sale of \$16.79 million of land with the Bay Area Rapid Transit District (BART).

SYSTEM PLANNING AND REGULATORY COMPLIANCE

The System Planning and Regulatory Compliance Bureau is responsible the development of medium and long range plans to maintain and improve water quality, water supply and wastewater treatment. These plans identify capital and operations improvements needed to ensure compliance with state and federal laws and regulations. The Bureau monitors and provides accountability for the regulatory compliance efforts of the various utilities.

HIGHLIGHTS FROM 1997-1998

Water Supply Master Plan – The Water Supply Master Plan is ongoing and identifies water supply strategies to address future San Francisco water needs of its wholesale water customers for the next 50 years. The Steering Committee, comprising of representatives from the SFPUC and its suburban wholesale customers, have agreed upon the potential need for future water and its desired level of water supply reliability. A range of water supply alternatives has been developed, with research into their potential contribution to improve water supply availability and reliability now underway. Concurrently, San Francisco and its wholesale customers are reviewing options for future water supplies to provide information for the Water Supply Master Plan to determine how much water will be purchased in the future from the SFPUC. This planning effort will continue throughout 1999.

Water Treatment Improvement Projects – Provided conceptual engineering for the conversion of the Hetch Hetchy water treatment to chloramine. Sunol Filter Plant conceptual engineering for near term improvements and capacity upgrades were approved by the SFPUC. Design of an auxiliary disinfection station at Thomas Shaft was completed. Preliminary engineering for the Peninsula Improvement Program is underway. The bond-funded project will seek to improve reliability of the Harry Tracy Plant and supporting system elements.

The Capital Improvement Program for the water system is estimated to cost \$2.36 billion:

Water quality = \$542 million (23%)

System reliability = \$1,596 million (67%)

Water supply = \$225 million (10%)



Capital Improvement Program – Completed the first comprehensive assessment of the capital improvements needs of the water system for the next 10 years. This report identified more than \$2.3 billion in needed improvements for system reliability, water quality and water supply.

Wastewater Master Plan – With activation of the Islais Creek Transport and Storage facility in March 1997, the Clean Water Program fully complies with its discharge permits for the first time in 20 years. San Francisco is one of the first cities in the country with a combined sewer system to complete its comprehensive wastewater management program.

ENVIRONMENTAL REGULATION AND MANAGEMENT

The Bureau of Environmental Regulation and Management is responsible for regulating industrial waste discharges to the sewer system, implementing the sewer user charge program, assisting the operating divisions in complying with environmental protection and industrial health and safety laws and regulations, and implementing health and safety programs for the entire SFPUC.

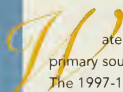
HIGHLIGHTS FROM 1997-1998

- Received the Public Education Award from the Water Environment Federation for promoting awareness and understanding of water quality issues.
- Helped assure effective management of the pretreatment program so that there were no violations at the wastewater treatment plants.
- Completed a three year pilot program that developed identification methodologies for potential storm water pollution sources, developed storm water pollution prevention strategies, and implemented storm water pollution prevention audits.
- Implemented the lockout/tagout program and assisted in the development of site specific procedures.
- Developed an Integrated Pest Management Plan for the SFPUC, which is became as a model for other City departments.
- Provided training to SFPUC personnel for the recognition and handling of hazardous waste.



Industrial Waste Inspector. San Francisco has pretreatment standards which prevent industries from discharging harmful amounts of wastes to sewers.

Economic Condition and Outlook



Water sales, sewer service charges, and power sales are the primary source of revenues for each of the respective enterprises. The 1997-1998 operating and capital expenditures were as follows: Water – \$137.4 million; Clean Water – \$144.6 million; and Hetch Hetchy – \$109.4 million.

The primary funding for capital projects for Water and Clean Water is from revenue bonds. Hetch Hetchy capital improvements are funded from current revenues. In November 1997, the voters of San Francisco approved an additional \$304 million in Water Revenue Bonds to fund capital projects for three years beginning in 1998-1999. The SFPUC expects to add commercial paper to its capital improvement financing structure in 1998-1999 to take advantage of low interest rates during construction. Over the next 15 years, plans are to complete capital improvement master plans of \$2.4 billion in Water, \$600 million in Clean Water, and \$250 million in Hetch Hetchy. Revisions to the Financial Master Plans to outline the funding for these capital improvements for the three enterprises will be completed during 1998-1999.

Due to voters' approval of Proposition H in June 1998, a water and sewer rate freeze is in effect until 2005-2006; consequently, during 1998-1999, finances are being totally reevaluated. Rates can only be increased for voter approved Revenue Bond Debt Service during this period. It is estimated that the Water enterprise will meet all its obligations without cost of living rate increases. The Clean Water enterprise outlook is not as optimistic. Approximately \$61 million in projected operating costs must be saved over the course of the next eight years in order for Clean Water to meet its future rate covenants to its bondholders. If the operating costs are not reduced, the shortfall is not predicted to occur until fiscal year 2001-02. Hetch Hetchy revenues are not part of the Proposition H implementation.

FINANCIAL SUMMARY

All of the utility functions of the SFPUC are accounted for as public service enterprise operations, which are financed and operated similarly to private business. Costs (including depreciation) of providing services to the general public are recovered in whole through user charges.

The following table presents the amount of revenues from various sources as well as increases or decreases from the prior years:

| Operating Revenues (In Thousands) | | | Increase/(Decrease) % of | |
|--------------------------------------|------------|------------|-----------------------------|--------|
| Revenue by source | FY 97-98 | FY 96-97 | Amount | Change |
| Charges for services | \$ 343,702 | \$ 336,387 | \$ 7,315 | 2.2 |
| Rental income | 6,381 | 5,412 | 969 | 17.9 |
| Other revenue | 2,070 | 2,180 | (110) | (5.0) |
| Total | \$ 352,153 | \$ 343,979 | \$ 8,174 | 2.4 |

The following provides an explanation of revenues by source, which changed significantly over the prior year.

- *Charges for Services* – The increase over the prior year is primarily due to an increase of approximately \$10 million in power sales at Hetchy due to the addition of IBM as a customer (which generated approximately \$9 million of revenue in FY98). The increase in power sales at Hetchy was partially offset by a reduction of approximately \$2.5 million in water sales to suburban customers due to the heavy rains during the spring and early summer.
- *Rental income* – The increase over the prior year is primarily due to increased rental activity during the year and rental increases from land leases owned by Water.

The following table presents operating expenses compared to prior year amounts.

| Operating Expenses (In Thousands) | | | Increase/(Decrease) % of | |
|--------------------------------------|------------|------------|-----------------------------|--------|
| Revenue by source | FY 97-98 | FY 96-97 | Amount | Change |
| Personnel services | \$ 88,292 | \$ 82,894 | \$ 5,398 | 6.5 |
| Contractual services | 31,831 | 29,768 | 2,063 | 6.9 |
| Light, heat and power | 10,032 | 11,222 | (1,190) | (10.6) |
| Materials and supplies | 11,815 | 13,170 | (1,355) | (10.3) |
| Depreciation & Amortization | 68,558 | 59,805 | 8,753 | 14.6 |
| General & administrative | 11,921 | 6,981 | 4,940 | 70.8 |
| Services provided by other depts. | 29,554 | 24,681 | 4,873 | 19.7 |
| Other | 21,057 | 11,784 | 9,273 | 78.7 |
| Total | \$ 273,060 | \$ 240,305 | \$ 32,755 | 13.6 |

An explanation of operating expenses that changed significantly over the prior year is as follows:

- *Personnel Services* - The increase from the prior year is primarily due to an increase of approximately 300 employees at the SFPUC during FY98. All new positions were funded for four to six months. Full funding is budgeted in 1998-99.
- *Contractual Services* - The increase over the prior year is primarily due to an increase of approximately \$2.7 million in purchased energy for resale by Hetch Hetchy from PG&E, and relate to the addition of IBM as a customer during FY98. The increase was partially offset by a reduction in building and structure maintenance costs of approximately \$900,000 at Hetch Hetchy and relates to the San Francisco International Airport Substation project.
- *Light, Heat & Power* - The decrease from the prior year is primarily due to a reduction of energy consumption by Water during FY98 of approximately \$1.2 million, and was the result of a concerted effort on the part of Water to reduce costs in gas and energy consumption.
- *Materials and Supplies* - The decrease from the prior year is primarily due to a general reduction in the consumption of materials and supplies by Water during FY98, and accounts for a decrease in materials and supplies cost of approximately \$1.4 million.
- *Depreciation and Amortization* - The increase over the prior year is primarily due to a significant increase in completed projects at Clean Water during FY97 and FY98 for which a full year of depreciation was taken during the current year for the projects completed during the prior year. One-half year's depreciation was recorded on projects completed in the current year. Of the three entities within the SFPUC, Clean Water realized an increase in depreciation expense of approximately \$6.8 million, Water realized an increase in depreciation expense of approximately \$1.6 million, and Hetch Hetchy realized an increase in depreciation expense of approximately \$0.4 million.
- *General and Administrative* - The increase over the prior year is primarily due to the change in the estimated claims liability at Water. During FY97, Water had decreased its estimated claims liability by approximately \$1.4 million. During FY98, Water increased its estimated claims liability by approximately \$3.2

million. The overall impact on general and administrative expense between FY97 and FY98 as a result of these adjustments was approximately \$4.6 million.

- *Services Provided by Other Departments* - The increase over the prior year is partially due to an increase in the shift in operational oversight of Clean Water from the Department of Public Works (DPW) to the SFPUC which resulted in an increase in "services provided by other departments" as Clean Water no longer resides or reports to the DPW. During the current year, Clean Water realized an increase in this category of approximately \$1.2 million, primarily relating to charges from the DPW. In addition, Water and Hetch Hetchy realized increased expenses of approximately \$3.7 million due to increased services provided by various City departments such as the City Attorney's Office, Mayor's Office and the Purchasing Department.
- *Other* - The increase over the prior year is primarily due to the write-off by Hetch Hetchy of the Tuolumne Sewage System for approximately \$3.5 million during FY98, an increase in bad debt expense of approximately \$1.2 million during FY98 by CWP, and an increase of approximately \$4.4 million in the level of project costs incurred during FY98 that were expensed given that the costs did not meet the SFPUC's capitalization criteria. The Tuolumne Sewage System Project involved constructing a sewage system in Yosemite National Park to eliminate the seepage of sewage from the park's sewage system into the Hetch Hetchy system reservoirs. Upon completion of the project, the constructed sewage system was contributed to the National Park Service.

The following table presents non-operating revenues and expenses as compared to prior year amounts:

Nonoperating Revenues and Expenses
(In Thousands)

| Revenue by source | FY 97-98 | FY 96-97 | Amount | Increase/(Decrease) % of |
|------------------------------|-------------|-------------|----------|-----------------------------|
| | | | | Change |
| Operating grant-federal | \$ 1,998 | \$ 1,588 | \$ 410 | 25.8 |
| Operating grant-state | 7,766 | - | 7,766 | 100.0 |
| Interest & investment income | 25,068 | 19,589 | 5,479 | 28.0 |
| Interest expense | (49,190) | (41,603) | (7,587) | (18.2) |
| Other, net | 799 | (957) | 1,756 | 183.5 |
| Total | \$ (13,559) | \$ (21,383) | \$ 7,824 | 36.6 |

The following explains non-operating revenues and expenses that changed significantly over the prior year.

- *Operating Grant - Federal* - The increase over the prior year is primarily due to additional revenue earned on the Treasure Island grant from the Navy.
- *Operating Grant - State* - The increase over the prior year is primarily due to an operating grant received by Clean Water from the state relating to storm damage which occurred in FY96 in the Seaclyff District of the City that resulted in damages to certain nearby homes.
- *Interest and Investment Income and Interest Expense* - The increase over the prior year is primarily due to a reduction in the amount of interest capitalized during FY98, primarily due to a reduction in construction activity.
- *Other Net* - The increase over the prior year is primarily due to the sale of certain leasehold rights by Water during FY98 which generated a gain from the sale of assets of approximately \$2.5 million, a gain from the surrender of leaseholds by Water during FY98 of approximately \$1.9 million, a loss due to the write-off of approximately \$5 million in construction projects at Clean Water during FY98, miscellaneous revenue of approximately \$1 million at Water and Hetch Hetchy during FY98, and a litigation claims loss of approximately \$1.6 million that occurred in FY97 and did not repeat in FY98. The \$5 million write-off by Clean Water was primarily related to the cross-town tunnel project that had been ongoing for several years and accounted for approximately \$3 million of Clean Water's write-off. The project was initiated as a result of a cease and desist order issued by the EPA, which required Clean Water to develop a means to reduce the discharge of treated affluent into the Bay. The project met considerable opposition from the residents of the City since its inception in early 1990's, and was abandoned in FY98 when the EPA issued an exception to the original cease and desist order, which eliminated the need for the tunnel.

The following table presents operating transfers as compared to prior year amounts:

Operating Transfers
(In Thousands)

| Revenue by source | FY 97-98 | FY 96-97 | Increase/(Decrease) | |
|-----------------------------------|-------------|-------------|---------------------|------|
| | | | Amount | % of |
| Operating transfers in | \$ 19,037 | \$ 19,037 | \$ - | 0.0 |
| Operating transfers out | (19,037) | (19,037) | - | 0.0 |
| Operating transfers from the City | 6,117 | 6,102 | 15 | 0.2 |
| Operating transfers to the City | (47,113) | (39,112) | 8,001 | 20.5 |
| Total | \$ (40,996) | \$ (33,010) | \$ 7,986 | 24.2 |

The following provides an explanation of operating transfers that changed significantly over the prior year.

- *Operating Transfers to City and County of San Francisco* - The increase over the prior year is primarily due to an increase of approximately \$8 million in the transfers from Hetch Hetchy to the City's General Fund. The transfers from Hetch Hetchy to the General Fund are based on budgeted amounts each year.

INTERNAL CONTROL STRUCTURE AND BUDGETARY CONTROLS

The Finance Division of the SFPUC is responsible for establishing and maintaining an internal control structure designed to ensure that the assets of the SFPUC are protected from loss, theft or misuse and to allow for the preparation of financial statements in conformity with generally accepted accounting principals. The internal control structure is designed to provide reasonable, but not absolute, assurance that these objective are met. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived, and (2) the valuation of cost and benefits requires estimates and judgments by management.

BUDGETARY CONTROLS

In addition, the SFPUC maintains budgetary controls, the objective of which is to ensure compliance with provisions embodied in the annual appropriated budgets approved by the SFPUC and Board of Supervisors. All financial activities are included in the annual operating budget, which are prepared in accordance with generally accepted accounting principals. Further, project-linked financial

plans are adopted in a separate capital projects budget. Function and activity within the San Francisco Charter and Administrative Code establish the level of budgetary controls. The General Manager has the discretion to transfer appropriations up to \$50,000 between functions and activities within and between divisions; however, the SFPUC and the Board of Supervisors approval is required for any overall increases in appropriation levels. The SFPUC also maintains an encumbrance system to aid in budgetary control. Encumbered accounts at year-end are reported as restricted and designated assets and are automatically reappropriated in the upcoming fiscal year. As demonstrated by the financial statements included in the financial section of this report, the SFPUC continues to meet its responsibility for sound financial management.

CASH MANAGEMENT

The SFPUC's pooled deposits and investments are invested pursuant to policy established by the City's Treasurer. This policy seeks the preservation of capital, liquidity and yield, in that order of priority. The policy addresses soundness of financial institutions holding our assets and the types of investments permitted by the California Government Code. The earned yield for the fiscal year 1997-98 was 6%. The SFPUC's non-pooled deposits and investments we invested pursuant to policy established by the SFPUC Commissioners.

RISK MANAGEMENT

The SFPUC is self-insured for General and Auto Liability. Property damage deductible coverage of \$750,000. The SFPUC maintains a Blanket Dishonesty Bond of \$20,000 deductible in force. The SFPUC's insurance/self-insurance program is reviewed annually in the budget process.

The SFPUC is self-insured for workers' compensation claims. A portion of the estimated cost is allocated to each department of the City according to a formula which considers claims payment history (experience) and payroll (exposure). This increases the visibility of workers' compensation issues in each department and creates financial accountability in the SFPUC. In order to better control the costs of workers' compensation, the City's Risk Management Office is working with SFPUC to develop workers' compensation programs tailored to our needs. The programs focus on accident prevention, investigation and a return-to-work modified duty program.

INDEPENDENT AUDIT

The SFPUC contracted for an annual audit of the books of accounts, financial records, and transactions of the SFPUC by KPMG Peat Marwick LLP and Yano & Associates, Certified Public Accountants. The audit has been completed and the firms' report has been included in the financial section of this report.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combined Financial Statements

June 30, 1998 and 1997

(With Independent Auditors' Report Thereon)

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

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Peat Marwick LLP

Yano & Associates

Independent Auditors' Report

Honorable Mayor and Board of Supervisors
City and County of San Francisco, California:

We have audited the combined financial statements of the San Francisco Public Utilities Commission (the Commission) as of and for the year ended June 30, 1998, as listed in the accompanying table of contents. These combined financial statements are the responsibility of the Commission's management. Our responsibility is to express an opinion on these combined financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 1, the financial statements present only the Commission and are not intended to present fairly the financial position of the City and County of San Francisco, California, and the results of its operations and the cash flows of its proprietary fund types in conformity with generally accepted accounting principles.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of the San Francisco Public Utilities Commission as of June 30, 1998, and the results of its combined operations and its combined cash flows for the years then ended in conformity with generally accepted accounting principles.

Our audit was performed for the purpose of forming an opinion on the combined financial statements of the San Francisco Public Utilities Commission taken as a whole. The combining financial statements listed in the table of contents are presented for purposes of additional analysis and are not a required part of the combined financial statements. Such information has been subjected to the auditing procedures applied in the audit of the combined financial statements and, in our opinion, is fairly stated in all material respects, in relation to the combined financial statements taken as a whole.

KPMG Peat Marwick LLP
Yano & Associates

San Francisco, California
October 23, 1998

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combined Balance Sheet

June 30, 1998
(with comparative amounts for June 30, 1997)
(dollars in thousands)

| Asset | 1998 | 1997 | Liabilities and Equity | 1998 | 1997 |
|---|------------------|------------------|--|--------------|--------------|
| Current assets: | | | Current liabilities: | | |
| Deposits and investments with City Treasury | \$ 178,798 | 155,959 | General obligation bonds, current portion | \$ 6,000 | 5,685 |
| Deposits and investments outside City Treasury | 390 | 124 | Revenue bonds, current portion | 23,430 | 119,260 |
| | | | State revolving loan funds, current portion | 10,904 | 10,186 |
| Receivables: | | | Accounts payable | 13,516 | 9,893 |
| Water, power, and sewer (net of allowance for doubtful accounts of \$2,482 in 1998 and \$1,242 in 1997) | 44,586 | 44,642 | Accrued payroll | 5,422 | 4,720 |
| Interest and other | 6,603 | 3,916 | Accrued vacation, sick leave, and workers' compensation, current payable | 6,001 | 5,519 |
| | | | Due to other funds | — | 393 |
| Total receivables | 51,189 | 48,558 | Bond interest payable | 12,478 | 13,881 |
| | | | Short-term debt | 7,370 | 9,722 |
| Due from other funds | — | 393 | Deferred revenue | 2,582 | 2,582 |
| | | | Damage and claims liability | 1,146 | 1,146 |
| Materials and supplies - at average cost | 1,052 | 1,787 | Deposits and construction advances | 1,471 | 1,919 |
| | | | Other | — | — |
| Total current assets | 231,429 | 206,821 | Total current liabilities | 97,671 | 185,375 |
| | | | Liabilities payable from restricted assets | 3,073 | 4,107 |
| Restricted assets: | | | Deferred revenue and other long-term liabilities: | | |
| Deposits and investments with City Treasury | 202,634 | 212,715 | Accrued vacation, sick leave, and workers' compensation | 6,733 | 6,474 |
| Deposits and investments outside City Treasury | 46,877 | 148,653 | Damage and claims liability | 2,580 | 7,843 |
| Interest receivable | 1,619 | 4,271 | Other | 150 | 204 |
| | | | Deferred revenue | 5,422 | 6,432 |
| Total restricted assets | 251,130 | 365,619 | Total deferred revenue and other long-term liabilities | 14,885 | 20,953 |
| | | | Long-term debt, less current portion: | | |
| | | | General obligation bonds | 830 | 6,830 |
| | | | Revenue bonds | 727,919 | 749,272 |
| | | | State revolving loan funds | 167,700 | 173,735 |
| | | | Total long-term debt | 896,449 | 929,837 |
| | | | Total liabilities | 1,012,078 | 1,140,272 |
| Net property, plant and equipment | 2,006,004 | 2,029,718 | Equity: | | |
| | | | Contributed capital | 630,758 | 644,909 |
| | | | Retained earnings—reserved for bond requirements and other commitments | 32,945 | 32,945 |
| | | | Retained earnings—unreserved | 828,193 | 789,774 |
| | | | Total equity | 1,461,896 | 1,467,628 |
| | | | Total equity and liabilities | \$ 2,463,974 | \$ 2,607,900 |
| Bond issuance costs, net of accumulated amortization of \$1,820 in 1998 and \$2,587 in 1997 | 5,411 | 5,742 | | | |
| Total assets | \$ 2,493,974 | \$ 2,607,900 | | | |

See accompanying notes to combined financial statements.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combined Statement of Income

For the year ended June 30, 1998

(with comparative amounts for the year ended June 30, 1997)

(dollars in thousands)

| | 1998 | 1997 |
|---|------------|----------|
| Operating revenues: | | |
| Charges for services | \$ 343,702 | 336,387 |
| Rental income | 6,381 | 5,412 |
| Other revenue | 2,070 | 2,180 |
| Total operating revenues | 352,153 | 343,979 |
| Operating expenses: | | |
| Personal services | 88,292 | 82,894 |
| Contractual services | 31,831 | 29,768 |
| Light, heat and power | 10,032 | 11,222 |
| Materials and supplies | 11,815 | 13,170 |
| Depreciation and amortization | 68,558 | 59,805 |
| General and administrative | 11,921 | 6,981 |
| Services provided by other departments | 29,554 | 24,681 |
| Other | 21,057 | 11,784 |
| Total operating expenses | 273,060 | 240,305 |
| Operating income | 79,093 | 103,674 |
| Nonoperating revenues (expenses): | | |
| Operating grant – federal | 1,998 | 1,588 |
| Operating grant – state | 7,766 | — |
| Interest and investment income | 25,068 | 19,589 |
| Interest expense | (49,190) | (41,603) |
| Other, net | 799 | (957) |
| Net nonoperating expenses | (13,559) | (21,383) |
| Income before operating transfers | 65,534 | 82,291 |
| Operating transfers: | | |
| Operating transfers in | 19,037 | 19,037 |
| Operating transfers out | (19,037) | (19,037) |
| Operating transfers from the City and County of San Francisco | 6,117 | 6,102 |
| Operating transfers to the City and County of San Francisco | (47,113) | (39,112) |
| Net operating transfers | (40,996) | (33,010) |
| Net income | \$ 24,538 | 49,281 |

See accompanying notes to combined financial statements.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combined Statement of Equity

For the year ended June 30, 1998

(with comparative amounts for the year ended June 30, 1997)

(dollars in thousands)

Contributed capital

| | Federal capital grants | State capital grants | Contribution from City and County of San Francisco | Retained earnings | Total |
|----------------------------|------------------------------|----------------------------|---|----------------------|------------------|
| Equity at July 1, 1996 | \$ 479,758 | 74,414 | 108,313 | 755,862 | 1,418,347 |
| Net income | — | — | — | 49,281 | 49,281 |
| Allocation of depreciation | (15,080) | (2,496) | — | 17,576 | — |
| Balances at June 30, 1997 | 464,678 | 71,918 | 108,313 | 822,719 | 1,467,628 |
| Net income | — | — | — | 24,538 | 24,538 |
| Write-off of fixed assets | (8,381) | (1,889) | — | — | (10,270) |
| Allocation of depreciation | (11,975) | (1,906) | — | 13,881 | — |
| Equity at June 30, 1998 | <u>\$ 444,322</u> | <u>68,123</u> | <u>108,313</u> | <u>861,138</u> | <u>1,481,896</u> |

See accompanying notes to combined financial statements.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combined Statement of Cash Flows

For the year ended June 30, 1998
(with comparative amounts for the year ended June 30, 1997)
(dollars in thousands)

| | 1998 | 1997 |
|---|------------|-----------|
| Cash flows from operating activities: | | |
| Cash received from customers, including cash deposits | \$ 341,722 | 338,526 |
| Cash received from tenants for rent | 6,381 | 5,412 |
| Cash paid to employees for services | (86,945) | (81,872) |
| Cash paid to suppliers for goods and services | (59,607) | (56,490) |
| Cash paid for quasi-external transactions | (50,542) | (44,370) |
| Net cash provided by operating activities | 151,009 | 161,206 |
| Cash flows from noncapital financing activities: | | |
| Operating grants | 9,764 | 1,588 |
| Operating transfers in | 20,447 | 20,446 |
| Operating transfers out | (66,150) | (58,149) |
| Other income received and property tax refund | — | 266 |
| Net cash used in noncapital financing activities | (35,939) | (35,849) |
| Cash flows from capital and related financing activities: | | |
| Bond issuance proceeds | — | 129,854 |
| Proceeds from sale of fixed assets | 2,537 | 116 |
| Federal and state capital grants | — | 58 |
| State revolving fund loan proceeds | 5,000 | 10,000 |
| Transfers from the City for debt service | 4,707 | 4,693 |
| Transfers to escrow to defease bonds | — | (57,012) |
| Interest and other bond costs paid | (52,430) | (47,248) |
| Principal paid on long-term debt | (124,945) | (25,470) |
| Principal paid on loans | (10,317) | (9,660) |
| Acquisition and construction of capital assets | (58,402) | (113,598) |
| Payment of capital lease obligations | (51) | (32) |
| Other capital financing increases | — | 173 |
| Other capital financing decreases | (1,182) | (5,676) |
| Net cash used in capital and related financing activities | (235,083) | (113,802) |
| Cash flows from investing activities: | | |
| Interest income received | 22,698 | 21,943 |
| Proceeds from sale of investments | 462,409 | 249,550 |
| Purchase of investments | (367,620) | (201,681) |
| Other investing activities | 4,440 | 1,779 |
| Net cash provided by investing activities | 121,927 | 71,591 |
| Increase in cash and cash equivalents | 1,914 | 83,146 |
| Cash and cash equivalents: | | |
| Beginning of year | 359,527 | 276,381 |
| End of year | \$ 361,441 | 359,527 |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combined Statement of Cash Flows

For the year ended June 30, 1998

(with comparative amounts for the year ended June 30, 1997)

(dollars in thousands)

| | 1998 | 1997 |
|---|------------|----------|
| Reconciliation of operating income to net cash provided by operating activities: | | |
| Operating income | \$ 79,093 | 103,674 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | |
| Depreciation and amortization | 68,558 | 59,805 |
| Provision for uncollectible accounts | 1,240 | — |
| Other | 3,260 | — |
| Changes in assets and liabilities: | | |
| Water, power, and sewer receivables, net | (1,184) | 849 |
| Due from other funds | 393 | (393) |
| Materials and supplies | 735 | 242 |
| Other receivables | (2,893) | (414) |
| Accounts payable | 3,623 | 524 |
| Accrued payroll | 702 | 1,197 |
| Accrued vacation, sick leave and workers' compensation | 741 | 374 |
| Due to other funds | (393) | 393 |
| Damage and claims liability | — | (1,421) |
| Deferred credits and other liabilities | (2,866) | (3,624) |
| Net cash provided by operating activities | \$ 151,009 | 161,206 |
| Reconciliation of cash and cash equivalents to the balance sheet: | | |
| Deposits and investments with City Treasury: | | |
| Unrestricted | \$ 178,798 | 155,959 |
| Restricted | 202,634 | 212,715 |
| Unrestricted deposits and investments outside City Treasury | 390 | 124 |
| Total deposits and investments | 381,822 | 368,798 |
| Add: Restricted deposits outside City Treasury meeting the definition of cash equivalents | 796 | 796 |
| Less: Deposits and investments not meeting the definition of cash equivalents | (21,177) | (10,067) |
| Cash and cash equivalents at end of year on combined statements of cash flows | \$ 361,441 | 359,527 |
| Noncash investing, capital and financing activities: | | |
| Write-off of fixed assets | (15,296) | — |
| Acquisition of fixed assets under capital lease agreement | — | 288 |
| Depreciation on contributed capital | 13,881 | 17,576 |
| | \$ (1,415) | 17,864 |

See accompanying notes to combined financial statements.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(1) The Financial Reporting Entity

The Public Utilities Commission (the Commission) was established in 1932, and is responsible for providing operational oversight of the public utility enterprises of the City and County of San Francisco (the City) which include the San Francisco Clean Water Program Fund Group (CWP), the San Francisco Water Department (SFWD) and the Hetch Hetchy Project (Hetchy). The PUC consists of five members who are appointed by the Mayor, and are responsible for determining such matters as the rates and charges for services, approval of contracts, and departmental policy. The combined financial statements of the Commission include the accounts of the CWP, SFWD, and Hetchy. The Commission is a department of the City and, as such, is included in the Comprehensive Annual Financial Report prepared by the City. The separate financial operations of the CWP and the combined financial operations of SFWD/Hetchy were reported on separately for the year ended 1997. A brief description of each of the entities governed by the Commission follows:

San Francisco Clean Water Program Fund Group

The CWP was established in 1977 following the transfer of all sewage system related assets and liabilities of the City on July 1, 1977 which was the first day of the fiscal year in which the San Francisco Series A Sewer Revenue Bonds of 1976 were issued.

In 1976, the electorate of the City approved a proposition authorizing the City to issue \$240 million in revenue bonds pursuant to the Revenue Bond Law of 1941 of the State of California for the purpose of acquiring, constructing, improving, and financing improvements to the City's municipal sewage treatment and disposal system. Since then, the Board of Supervisors of the City has adopted resolutions (the Clean Water Resolutions) providing for the issuance of various sewer revenue and refunding bond series. As of June 30, 1993, the City exhausted its bonding capacity under the 1976 proposition approved by the electorate. The Clean Water Resolutions require the City to keep separate books of record and accounts.

San Francisco Water Department

The SFWD was established in 1930 under the provisions of the City Charter of San Francisco. The SFWD acquired the fully developed, mature water works for San Francisco on March 3, 1930. Since then, the City has operated and maintained the water works as the SFWD. The Board of Supervisors of the City has adopted resolutions (the Water Resolutions) providing for the issuance of various water revenue and refunding bond series. The SFWD is engaged in the distribution of water to San Francisco and certain suburban areas.

Hetch Hetchy Project

Hetchy originated as a result of the Raker Act of 1913, which granted water and power resources rights-of-way on the Tuolumne River in Yosemite National Park to the City of San Francisco. Hetchy is engaged in the collection and distribution of water to the SFWD and in the generation and transmission of electricity to San Francisco.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(2) Significant Accounting Policies

(a) Basis of Accounting — Fund Accounting

The accounts of the Commission are organized on the basis of an enterprise fund type. The operations of each fund (the CWP, SFWD and Hetchy) are accounted for with a separate set of self-balancing account that comprises their assets, liabilities, fund equity, revenues, and expenses. Enterprise Funds account for operations (a) that are financed and operated in a manner similar to private business enterprises where the intent of the Board of Commissioners is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or (b) where the Board of Commissioners has decided that periodic determination of revenues earned, expenses incurred, and net income or loss is appropriate for capital maintenance, public policy, management control, accountability, or other purpose.

(b) Measurement Focus

The financial activities of the Commission are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Under this method, all assets and liabilities associated with operations are included on the balance sheet; revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

Eliminations of interfund activity have been made within funds but not within the fund type.

The Commission does not apply Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989. The Commission applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as statements and interpretations of FASB, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

(c) Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid investments, including restricted assets, with an original purchased maturity of three months or less.

(d) Investments

Certain investments are stated at fair value based upon quoted market prices. Changes in fair value are recognized as investment income.

Money market funds and banker's acceptances that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(e) Inventory

Inventory primarily consists of construction materials and maintenance supplies and is generally valued at cost or average cost. Inventory is expensed as it is consumed.

(f) Property, Plant and Equipment

San Francisco Clean Water Program Fund Group

Property, plant and equipment with an original acquisition date prior to July 1, 1977 are recorded in the financial statements at estimated cost, as determined by an independent professional appraisal, or at cost, if known. All subsequent acquisitions have been recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets which range from 4 to 75 years. One-half year's depreciation is recorded during the first year of operation which approximates asset utilization.

The portion of depreciation relating to completed assets financed by capital grants is closed to federal and state contributed capital grant equity.

San Francisco Water Department and Hetch Hetchy Project

Property, plant and equipment is stated at cost. Depreciation and amortization are computed by using the straight-line method based on the estimated useful lives of the related assets, which range from 3 to 75 years for equipment and 3 to 173 years for buildings, structures and improvements. No depreciation or amortization is recorded in the year of acquisition and a full year's depreciation or amortization is recorded in the year of disposal.

(g) Construction in Progress

The cost of acquisition and construction of major plant and equipment is recorded as construction in progress. As facilities are accepted by the Commission and become operative, they are transferred to the plant and equipment accounts and depreciated in accordance with the Commission's depreciation policies. Costs of projects which are discontinued are recorded as expense in the year in which the decision is made to discontinue the project.

(h) Capitalization of Interest

A portion of the interest cost incurred on capital projects is capitalized on assets which require a period of time for construction or to otherwise prepare them for their intended use. Such amounts are amortized over the useful lives of the assets.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(i) Bond Discount and Issuance Costs

Bond discount and issuance costs are amortized over the term of the related bonds.

(j) Accrued Vacation, Sick Leave, and Workers' Compensation

Accrued vacation pay, which may be accumulated up to ten weeks per employee, is charged to expense as earned. Unused sick leave accumulated through December 6, 1978 is vested and payable upon termination of employment by retirement, death, or disability caused by industrial accident. Sick leave earned subsequent to that date is nonvesting and may be accumulated up to six months per employee. The Commission is self-insured for workers' compensation claims and accrues the estimated cost of those claims, including the cost of incurred but not reported claims.

(k) Damage and Claims Liability

The Commission is self-insured for general liability and property damage claims. The liability represents an estimate of the cost of all outstanding claims and incurred but not reported claims.

(l) Arbitrage Rebate Payable

Certain bonds are subject to an arbitrage rebate requirement in accordance with regulations issued by the U.S. Treasury Department. The requirements stipulate, in general, that earnings from the investment of the tax-exempt bond proceeds that exceed related interest costs on the bonds must be remitted to the federal government on every fifth anniversary of each bond issue. As of June 30, 1998, the arbitrage rebate liability was approximately \$441. As of June 30, 1997, there was no arbitrage rebate liability.

(m) Refunding of Debt

Gains or losses occurring from advance refundings are deferred and amortized into interest expense over the remaining life of the old bonds or the life of the new bonds, whichever is shorter.

(n) Income Taxes

As a government agency, the Commission is exempt from both federal income taxes and California state franchise taxes.

(o) Contribution from the City and County of San Francisco

The net book value of all assets and liabilities, including liabilities under sewage-related general obligation bonds relating to the sewage system transferred from the City to the CWP, are reflected as contributed capital in the combined financial statements.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(p) *Revenue Recognition*

Sewer service charges are based on water usage as determined by the SFWD. Billings are on a monthly or bimonthly basis. Revenues reflected in the financial statements include accruals based on estimates for the periods between termination of the billing cycle and the end of the fiscal year.

Sewer revenue rates must be set to produce sufficient revenue to fund the obligations of the CWP as defined in the Clean Water Resolutions, including costs for operation, maintenance, repair and replacements, revenue bond debt service and compliance with federal and state laws and regulations. In addition, City Ordinance No. 198-77 requires that rates be recommended annually to produce sufficient revenue (except to the extent that funds are provided by transfers from other City funds – note 11) to pay debt service on sewage-related general obligation bonds (note 14).

Revenues from water and power services furnished to consumers are recorded in the combined financial statements in the period that meters are read. In general, customers are billed on a cyclical basis with large commercial and industrial customers billed monthly and all other customers bimonthly.

(q) *Use of Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(r) *Reclassifications*

Certain reclassifications have been made to the 1997 financial statements to conform to the 1998 presentation. These reclassifications did not change total assets, liabilities, equity or net income.

(3) **Cash and Investments**

The captions on the balance sheet related to cash and investments at June 30 are as follows:

| | 1998 | 1997 |
|---|-------------------|----------------|
| Deposits and investments with City Treasury: | | |
| Unrestricted — pooled | \$ 178,798 | 155,959 |
| Restricted — pooled and nonpooled (note 5) | 202,634 | 212,715 |
| Deposits and investments outside City Treasury: | | |
| Unrestricted | 390 | 124 |
| Restricted (note 5) | 46,877 | 148,633 |
| | <u>\$ 428,699</u> | <u>517,431</u> |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

Investments

The Commission's equity in deposits and investments of the City Treasurer is invested pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy guidelines are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The Comprehensive Annual Financial Report of the City categorizes the level of custodial risk associated with the City's pooled cash and investments which includes \$293,998 and \$318,739 of the Commission's total equity in deposits and investments of the City Treasurer as of June 30, 1998 and 1997, respectively. The City Treasurer allocates monthly income from the investment of pooled cash in proportion to the end-of-month balances held by the Commission.

The CWP and SFWD are required by their bond indentures to maintain certain revenue bond funds in government obligations, time deposits, or demand deposits. The Commission follows the investment policy guidelines of the City Treasurer for its other investments, including those investments held by trustees.

The investments of the Commission, including those held by trustees, are categorized below to give an indication of the level of custodial risk assumed at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the Commission or its agent in the name of the Commission. Category 2 includes uninsured and unregistered investments for which the securities are held by the counter-party's trust department or agent in the name of the respective entity. Category 3 includes uninsured and unregistered investments for which the securities are held by the counter-party, or by its trust department or agent but not in the name of the respective entity.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

The investment portfolio of the Commission is stated at fair value (except for money market funds and banker's acceptances which are stated at amortized cost which approximates market) and is based on quotes obtained from national exchanges as of June 30, 1998.

| | Category | | | Carrying value |
|---|-------------------|----------|----------|-------------------|
| | 1 | 2 | 3 | |
| Banker's acceptances | \$ 57,145 | — | — | 57,145 |
| U.S. Treasury bills | 37,322 | — | — | 37,322 |
| U.S. Treasury notes | 969 | — | — | 969 |
| Commercial paper | 25,793 | — | — | 25,793 |
| Other U.S. Government securities | 12,626 | — | — | 12,626 |
| | <u>\$ 133,855</u> | <u>—</u> | <u>—</u> | 133,855 |
| Money market funds | | | | 796 |
| Imprest Fund | | | | 50 |
| Pooled cash and investments held by the City Treasurer | | | | <u>293,998</u> |
| | | | | <u>\$ 428,699</u> |

(4) Property, Plant and Equipment

Property, plant and equipment at June 30, 1998 and 1997 consisted of the following:

| | 1998 | 1997 |
|--|---------------------|------------------|
| Land | \$ 43,627 | 43,837 |
| Buildings, structures and improvements | 2,732,611 | 2,630,082 |
| Equipment | 85,491 | 82,531 |
| Construction-in-progress | 65,648 | 126,023 |
| | <u>2,927,377</u> | <u>2,882,473</u> |
| Less accumulated depreciation and amortization | <u>(921,373)</u> | <u>(852,755)</u> |
| | <u>\$ 2,006,004</u> | <u>2,029,718</u> |

During the years ended June 30, 1998 and 1997, the Commission incurred total interest expense of \$52,300 and \$50,114, respectively. Of the total amount of interest expense incurred, \$3,110 and \$8,511 was capitalized into the cost of constructed assets during the years ended June 30, 1998 and 1997, respectively.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

During fiscal year 1998, the CWP wrote-off fixed assets totaling approximately \$15.3 million. Included in the amount written-off was approximately \$13.8 million relating to the cross-town tunnel project which would have connected the Bayside and Oceanside Sewage Treatment Plants. This project was originally initiated as a result of the cease and desist order issued by the Environmental Protection Agency (EPA); however, during fiscal year 1998 the EPA amended the original cease and desist order which eliminated the need for the completion of the project. The remaining \$1.5 million of write-offs pertained to design and planning costs on certain projects which were discontinued during fiscal year 1998. Of the amount written-off, \$10.3 million were assets acquired by capital grant funding which resulted in a reduction of contributed capital. The remaining \$5 million was recognized as other nonoperating expense.

(5) Restricted Assets

Pursuant to the Clean Water Resolution and Water Resolution, all revenue of the CWP and SFWD (except amounts on deposit in the rebate fund) are irrevocably pledged to the punctual payment of debt service on the respective Sewer Revenue and Refunding Bonds and the Water Revenue and Refunding Bonds. Accordingly, the revenues of either entity shall not be used for any other purpose while any of their respective Revenue and Refunding Bonds are outstanding except as expressly permitted by the respective Resolutions. Further, all revenues shall be deposited by the City Treasurer in special funds designated as the Sewer Service Revenue Fund (the Sewer Revenue Fund) and the Water Department Revenue Fund (the Water Revenue Fund) which must be maintained in the City Treasury. Deposits in the Sewer Service Revenue and Water Revenue Funds, including earnings thereon, shall be appropriated, transferred, expended or used for the following purposes pertaining to the financing, maintenance and operation of the CWP and SFWD in accordance with the following priority:

(a) *San Francisco Clean Water Program Fund Group*

1. The payment of State loans;
2. The payment of maintenance and operation costs of the CWP;
3. The payment of fees and expenses of the Fiscal Agent and payment of the periodic fees, if any, payable to any Reserve Provider or Credit Provider in conjunction with the Bonds;
4. The payment of amounts required to be deposited into the Principal Fund, Interest Fund, Bond Reserve Fund, Sinking Fund Accounts, and any other mandatory funds and accounts created to secure Bonds issued by the City for the financing or the refinancing of the acquisition, construction or extension of the CWP;
5. The payment of, or deposit into, the debt service, reserve and other mandatory funds and accounts created to secure, obligations of the City payable from net revenues for the financing or refinancing of the CWP which are subordinated to the Bonds;
6. Any deposits required to be made into the Repair and Replacement Fund pursuant to the Resolution;

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

7. Any deposit to be made into the Working Capital Fund pursuant to the Clean Water Resolution.
8. Any deposit to be made into the Rate Stabilization Fund pursuant to the Clean Water Resolution; and,
9. Any deposit to be made into the Surplus Revenue Fund pursuant to the Clean Water Resolution.

(b) *San Francisco Water Department*

1. The payment of operation and maintenance expenses for such utility and related facilities;
2. The payment of pension charges and proportionate payments to such compensation and other insurance or outside reserve funds as the Commission may establish or the Board of Supervisors may require with respect to employees of the Commission;
3. The payment of principal, interest, reserve, sinking fund, and other mandatory funds created to secure Revenue Bonds issued by the Commission for the acquisition, construction or extension of SFWD or related facilities owned, operated or controlled by the Commission;
4. The payment of principal and interest on General Obligation Bonds issued by the City for SFWD purposes;
5. Reconstruction and replacement as determined by the Commission or as required by any SFWD Revenue Bond ordinance duly adopted and approved; and,
6. The acquisition of land, real property or interest in real property for, and the acquisition, construction, enlargement and improvement of, new and existing buildings, structures, facilities, equipment, appliances and other property necessary or convenient to the development or improvement of such utility owned, controlled or operated by the Commission; and for any other lawful purpose of the Commission including the transfer of surplus funds pursuant to Section 6.407(e) of the City's Charter.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

In accordance with the Clean Water Resolution and the Water Resolution, the CWP and SFWD maintain certain restricted cash and investment balances in trust. Restricted assets held in trust consisted on the following at June 30, 1998 and 1997:

| | 1998 | 1997 |
|---|------------|---------|
| Equity in deposits and investments of the City Treasurer: | | |
| 1972 Water Bond Fund | \$ — | 467 |
| Water Bond Construction Fund | 74,348 | 83,271 |
| Sewer Bond Construction Fund | 128,286 | 128,977 |
| Total | 202,634 | 212,715 |
| Investments held by trustee: | | |
| 1987 Water Revenue Bond Fund | — | 4,088 |
| 1991 Water Revenue Bond Fund | 3,700 | 3,763 |
| 1992 Water Revenue Bond Fund | 3,459 | 99,580 |
| 1996 Water Revenue Bond Fund | 1,992 | 4,105 |
| 1991 Sewer Revenue Bond Fund | 2,778 | 2,681 |
| 1992 Sewer Revenue Refunding Bond Fund | 18,783 | 18,251 |
| 1994 Sewer Revenue Refunding Bond Fund | 15,369 | 15,369 |
| 1995 Sewer Revenue Bond Fund | 796 | 796 |
| Total | 46,877 | 148,633 |
| Interest receivable: | | |
| 1972 Water Bond Fund | — | 7 |
| Water Bond Construction Fund | 545 | 2,346 |
| Sewer Bond Construction Fund | 1,074 | 1,918 |
| Total | 1,619 | 4,271 |
| Total restricted assets | \$ 251,130 | 365,619 |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(6) Long-Term Debt

The Commission's long-term debt consisted of the following at June 30, 1998 and 1997:

| | Interest rates | Due serially to | 1998 | 1997 |
|--|----------------|--------------------|------------|-----------|
| General obligation bonds: | | | | |
| 1970 Water Pollution Control Bonds – Series D | 4.00% – 6.00% | 1999 | \$ 2,770 | 5,385 |
| 1972 Sewer System Improvement Bonds – Series C | 4.00% – 6.00% | 1999 | 1,890 | 3,675 |
| 1972 Municipal Water System Bonds | 4.00% – 5.70% | 2000 | 2,170 | 3,455 |
| Total general obligation bonds | | | 6,830 | 12,515 |
| Less current portion of general obligation bonds | | | (6,000) | (5,685) |
| Long-term portion of general obligation bonds | | | \$ 830 | 6,830 |
| Revenue Bonds: | | | | |
| 1991 Sewer Revenue Bonds | 5.75% – 6.50% | 2003 | 15,750 | 18,359 |
| 1992 Sewer Revenue Refunding Bonds | 5.50% – 6.00% | 2016 | 280,380 | 295,080 |
| 1994 Sewer Revenue Refunding Bonds | 4.70% – 5.80% | 2023 | 174,980 | 174,981 |
| 1995A Sewer Revenue Bonds | 5.38% – 5.95% | 2026 | 44,230 | 44,230 |
| 1995B Sewer Revenue Bonds | 5.55% – 5.95% | 2011 | 13,376 | 12,638 |
| 1987 Water Revenue Refunding Bonds | 6.65% – 8.50% | 1998 | — | 100,596 |
| 1991 Water Revenue Bonds | 5.30% – 7.40% | 2021 | 11,659 | 12,886 |
| 1992 Water Revenue Refunding Bonds | 5.35% – 6.50% | 2016 | 107,180 | 107,180 |
| 1996 Water Revenue Refunding Bonds | 5.00% – 6.50% | 2026 | 131,455 | 131,470 |
| Unamortized bond discount and refunding loss | | | (27,661) | (28,888) |
| Total revenue bonds | | | 751,349 | 868,532 |
| Less current portion of revenue bonds | | | (23,430) | (119,260) |
| Long-term portion of revenue bonds | | | \$ 727,919 | 749,272 |

The payments of principal and interest amounts on various bonds are collateralized by future sewer and water revenues.

(a) General Obligation Bonds

Pursuant to City policy, the CWP is obligated to pay the principal and interest of General Obligation Bonds of the City that relate to sewage and water pollution control. The bonds have interest rates that

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

range from 4% to 6% and mature annually through fiscal year 1999. If the CWP's revenues are not sufficient to make these payments, the City must make the payments from other sources.

During 1972, the SFWD issued \$39,000 of general obligation bonds relating to the municipal water system. The bonds have interest rates ranging from 4.0% to 5.7% and mature annually through 2000.

The future annual debt service relating to the General Obligation Bonds outstanding at June 30, 1998 is as follows:

| | <u>Principal</u> | <u>Interest</u> |
|------------------------------------|------------------|-----------------|
| Year ending June 30: | | |
| 1999 | \$ 6,000 | 159 |
| 2000 | 830 | 19 |
| | <u>6,830</u> | <u>\$ 178</u> |
| Less: Current portion | <u>6,000</u> | |
| Long-term portion at June 30, 1998 | <u>\$ 830</u> | |

The Commission has complied with the debt covenants of the General Obligation Bonds.

(b) General Purpose Sewer Revenue Bonds Series 1991

In July 1991, the Board of Supervisors of the City adopted resolutions providing for the issuance of \$170,000 General Purpose Sewer Revenue Bonds (Series 1991). Interest rates for the issue vary from 5.75% to 6.50%.

The Series 1991 Bonds were issued without voter approval as such bonds were to be used to finance facilities under Cease and Desist Orders from the San Francisco Bay Regional Water Quality Control Board (the Regional Board). The bonds are payable solely from pledged revenues of the CWP and are not payable from any other source.

On March 2, 1994 Sewer Revenue Refunding Bonds Series 1994 were issued with a face value of approximately \$175,000 of which net proceeds were used to refund approximately \$144,700 of the Series 1991 Bonds in a legal defeasance (note 6d).

(c) Sewer Revenue Refunding Bonds Series 1992

On August 4, 1992, the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Refunding Bonds Series 1992 (the 1992 Refunding Bonds) in the principal amount of approximately \$331,000 with interest rates varying from 5.5% to 6.0% maturing serially through October 1, 2015.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(d) Sewer Revenue Refunding Bonds Series 1994

On January 24, 1994, the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Refunding Bonds Series 1994 (the 1994 Refunding Bonds) in the principal amount of \$174,980 with interest rates varying from 4.7% to 5.38%. Interest-only payments are due semi-annually on April 1 and October 1 of each year until April 1, 2000, at which time the bonds begin to mature serially through October 1, 2022.

(e) Sewer Revenue Bonds, Series 1995

On November 8, 1994, voters approved the issuance of Sewer Revenue Bonds in the amount of approximately \$146,100. On May 8, 1995 the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Bonds Series 1995A and 1995B (the 1995 Bonds). The Series 1995A Bonds have a principal amount of approximately \$44,200 with interest varying from 5.38% to 5.95% and mature serially through October 1, 2025. Interest payments are due semiannually on April 1 and October 1 of each year. The Series 1995B Bonds have a principal amount of approximately \$11,300 with interest varying from 5.55% to 5.95% and mature serially from October 1, 2006 through October 1, 2010. Interest payments are due semi-annually beginning October 1, 2006 through October 1, 2010. The CWP recognizes annual interest expense on the Series 1995B Bonds over the life of the Bonds using the interest method. The CWP has recognized approximately \$2,100 and \$1,400 of unpaid interest on the Series 1995B Bonds at June 30, 1998 and 1997, respectively, and has included it with the outstanding principal balance of the Series 1995B Bonds. The Series Revenue Bonds were issued for the purpose of providing funds for certain improvements to the City's sewage treatment and disposal system.

(f) Water Revenue Refunding Bonds Series 1987

During the fiscal year 1987, the SFWD issued Revenue Refunding Bonds of approximately \$106,117 with interest varying from 6.10% to 8.50%. The Refunding Bonds include current interest serial and term bonds of approximately \$92,985 and serial and term capital appreciation bonds with an original principal amount of approximately \$13,132. The current interest serial bonds mature through November 1, 2006 and the current interest term bonds mature on November 1, 2011. The serial capital appreciation bonds mature from November 1, 1990 through November 1, 2002 and the term capital appreciation bonds mature on November 1, 2007 and 2015. Interest on the capital appreciation bonds is due upon maturity, and is recognized as annual interest expense over the life of the Bonds using the interest method. The SFWD had recognized approximately \$14,444 of unpaid interest on the capital appreciation bonds at June 30, 1997 and had included it with the outstanding principal balance of the Bonds. During fiscal year 1998, the SFWD advance refunded the outstanding principal balance and accrued interest of the 1987 Refunding Bonds with the remaining proceeds from the 1992 refunding bonds (note 6h).

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(g) *Water Revenue Bonds Series 1991*

During fiscal year 1991, the SFWD issued Revenue Bonds of approximately \$70,146 with interest varying from 5.00% to 7.40%. The Revenue Bonds include current interest serial and term bonds of approximately \$92,985 and serial capital appreciation bonds with an original principal amount of approximately \$1,051. The current interest serial bonds mature through November 1, 2007 and the current interest term bonds mature on November 1, 2010, 2017 and 2020. The serial capital appreciation bonds mature from November 1, 2018 through November 1, 2019. Interest on the capital appreciation bonds is due upon maturity, and is recognized as annual interest expense over the life of the Bonds using the interest method. The SFWD has recognized approximately \$647 and \$534 of unpaid interest on the capital appreciation bonds at June 30, 1998 and 1997, respectively, and has included it with the outstanding principal balance of the Bonds.

(h) *Water Revenue Refunding Bonds Series 1992*

In fiscal 1992, the SFWD issued \$107,180 of Revenue Bonds pursuant to a crossover refunding of 1987 Water Revenue Refunding Bonds. The proceeds were used to purchase U.S. government securities which were placed into an irrevocable trust to be used for the payment of interest on the 1992 Refunding Bonds and \$460 per year of principal due on the 1987 Refunding Bonds through November 1, 1997 (crossover date), at which time the remaining proceeds were used to advance refund the 1987 Refunding Bonds. The debt service requirements of the 1992 Revenue Bonds after the crossover date will be made from the net revenues of the SFWD.

(i) *Water Revenue Refunding Bonds Series 1996*

In fiscal 1997, the SFWD issued \$131,470 (face value) of 1996 Series A Water Revenue Bonds. A portion of the bond proceeds was designated for the purpose of refunding \$53,090 (face value) of 1991 Revenue Bonds which were due serially to 2020. The funding extended maturities on the bonds in order to lower required annual payments. After payment of \$852 in issue costs, \$57,012 of the net bond proceeds was transferred to a trustee to be placed in an irrevocable trust to redeem the refunded portion of the 1991 Revenue Bonds. Accordingly, the refunded portion of the 1991 Revenue Bonds was removed from the SFWD's balance sheet. The advance refunding decreased the SFWD's total debt service payment over the next 29 years by \$2,475 and provided for an economic gain of \$4,064. The resulting accounting loss of \$5,989 had been deferred and is being amortized over the remaining life of the old debt.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(j) *Future Annual Debt Service of Revenue Bonds*

The future annual debt service relating to the Revenue Bonds outstanding at June 30, 1998 is as follows:

| | <u>Principal</u> | <u>Interest</u> |
|--|--------------------------|--------------------------|
| Year ending June 30: | | |
| 1999 | \$ 23,430 | 42,654 |
| 2000 | 26,465 | 41,290 |
| 2001 | 29,230 | 39,767 |
| 2002 | 30,905 | 38,141 |
| 2003 | 32,705 | 36,400 |
| Thereafter | <u>636,275</u> | <u>331,918</u> |
| | 779,010 | \$ <u><u>530,170</u></u> |
| Less: | | |
| Current portion | (23,430) | |
| Unamortized bond discount and refunding loss | <u>(27,661)</u> | |
| Long-term portion at June 30, 1998 | \$ <u><u>727,919</u></u> | |

As defined in the Clean Water Resolution and Water Resolution, the principal and interest of the Revenue and Refunding Bonds of the CWP and SFWD are payable from the corresponding revenue of the respective entities and from monies deposited in certain funds and accounts pledged thereto (note 5).

The Commission has complied with the debt covenants of the Revenue Bonds.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(7) State Revolving Fund Loans

The CWP entered into several contracts with the California State Water Resources Board (SWRCB) under which the CWP can borrow up to prescribed maximum amounts to finance the construction of certain facilities. Loans outstanding at June 30, 1998 are summarized as follows:

| Project | Date of loan | Maturity date | Interest rate | Amount outstanding | Maximum loan amount |
|--------------|--------------|---------------|---------------|--------------------|---------------------|
| Oceanside | 07/25/90 | 2010 | 3.4% | \$ 28,524 | 40,000 |
| Oceanside | 06/10/91 | 2011 | 3.5% | 23,080 | 32,376 |
| Mariposa | 01/10/91 | 2011 | 3.5% | 5,472 | 7,624 |
| Oceanside | 04/28/92 | 2007 | 3.5% | 27,594 | 42,200 |
| Mariposa | 11/01/91 | 2011 | 3.1% | 1,473 | 1,936 |
| Lake Merced | 02/05/92 | 2012 | 3.1% | 16,045 | 21,114 |
| Islais Creek | 10/08/92 | 2012 | 3.0% | 4,549 | 5,706 |
| Oceanside | 12/24/93 | 2012 | 2.9% | 11,975 | 14,100 |
| Islais Creek | 09/07/93 | 2012 | 3.1% | 22,524 | 26,800 |
| Islais Creek | 06/17/94 | 2013 | 2.9% | 13,537 | 15,000 |
| Islais Creek | 06/13/96 | 2015 | 3.4% | 9,292 | 10,000 |
| Rankin Pump | 12/23/96 | 2017 | 3.1% | 14,539 | 15,000 |
| | | | | <u>\$ 178,604</u> | <u>231,856</u> |

Repayment of interest and principal shall be by installments with the final amount due from 15 to 20 years after the first disbursement by SWRCB. Disbursements are made by SWRCB as funds are spent for the projects. The CWP is required to comply with applicable federal and state regulations. The future annual debt service relating to the Revenue Bonds outstanding at June 30, 1998 is as follows:

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

| | <u>Principal</u> | <u>Interest</u> |
|------------------------------------|-------------------|------------------|
| Year ending June 30: | | |
| 1999 | \$ 10,904 | 5,678 |
| 2000 | 11,164 | 5,418 |
| 2001 | 11,530 | 5,052 |
| 2002 | 11,909 | 4,673 |
| 2003 | 12,300 | 4,282 |
| Thereafter | 120,797 | 20,932 |
| | <u>178,604</u> | <u>\$ 46,035</u> |
| Less current portion | <u>(10,904)</u> | |
| Long-term portion at June 30, 1998 | <u>\$ 167,700</u> | |

(8) Suburban Water Rate Agreement

On July 1, 1984, certain suburban customers entered into an agreement that establishes water rates to be charged to the suburban customers. In accordance with the agreement, the water rates are calculated based on a prescribed allocation of expenses and an allowed rate of return on certain water related assets. During fiscal year 1998 and 1997, the suburban revenue requirement charged to such suburban customers was \$63,917 and \$52,154, respectively. Such amounts are subject to final review by the suburban customers based on the suburban revenue requirement calculation. The liability to the suburban customers was approximately \$7,400 and \$9,700 at June 30, 1998 and 1997, respectively, relating to the suburban rate agreement.

(9) Deferred Revenue

Deferred revenue consists of an upfront fee received by the CWP during the 1994-95 fiscal year.

In January 1995, the CWP entered into a forward purchase and sale agreement with an investment bank (the Bank). Under the agreement, the CWP received an upfront fee of approximately \$8,900 from the Bank. In exchange, the CWP will use its debt service payments deposited but not yet due to bondholders to purchase short-term U.S. Treasury bills from the Bank at face value.

The upfront fee was deposited into the CWP's Rate Stabilization Fund and recorded as deferred revenue in the accompanying financial statements. Revenue is being recognized over the life of the agreement based on the present value of the future earnings. The unamortized balance at June 30, 1998 and 1997 is approximately \$5,400 and \$6,400, respectively.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

(10) Employee Benefits

(a) Retirement Plan

Plan Description — The City has a single-employer defined benefit retirement plan (the Plan) which is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). The Plan covers substantially all full-time employees of the Commission along with other employees of the City. The Plan provides basic service retirement, disability and death benefits based on specified percentages of final average salary and provides cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City and County Employees' Retirement System, 1155 Market Street, 2nd Floor, San Francisco, CA 94103 or by calling (415) 554-1520.

Funding Policy — Contributions are made to the basic payroll plan by both the Commission and its employees. Employee contributions are mandatory. Employee contribution rates for 1998 varied from 7% to 8% as a percentage of covered payroll. The Commission is required to contribute at an actuarially determined rate. No Employer contributions were required in 1998. The Commission's contributions to the San Francisco City and County Employees' Retirement System on behalf of employees for the years ending June 30, 1998, 1997 and 1996 were approximately \$3,320, \$2,987 and \$3,585, respectively, equal to the required contributions for the year.

(b) Health Care Benefits

Health care benefits of Commission employees, retired employees and surviving spouses are financed by beneficiaries and by the City through the City and County of San Francisco Health Service System, an internal service fund. The Commission's contributions covering current and retired employees, which amounted to approximately \$1,200 in fiscal years 1998 and 1997, respectively, is determined by Charter provisions based on similar contributions made by the ten most populous counties in California. The Commission's liability for both current employee and postretirement health care benefits is limited to its annual contribution.

(11) Related Parties

Included in 1998 and 1997 operating revenues are sales of power to departments within the City of \$41,234 and \$42,455, respectively. Sales of water delivered without charge to certain City departments of \$5,317 and \$5,032, respectively, are not included in operating revenues.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

Income from Hetchy is available for certain operations of the City. During the years ended June 30, 1998 and 1997, Hetchy transferred \$45,703 and \$30,165, respectively, to the General Fund. During the year ended June 30, 1997, Hetchy also transferred \$7,538 to the San Francisco Municipal Railway (Muni) to fund certain maintenance and repair costs relating to Muni's overhead lines. During the year ended June 30, 1998 Hetchy transferred Muni's share of funding to the General Fund which in turn provides an annual operating subsidy to Muni to fund certain operational costs.

Effective July 1, 1996, the Commission assumed responsibility for certain overhead costs previously incurred by the individual departments under its control. These costs are now allocated back to the CWP, SFWD, and Hetchy. For the year ended June 30, 1998 and 1997, the Commission allocated \$18,442 and \$10,902, respectively, in overhead expenses to the CWP, SFWD and Hetchy.

The City performs certain administrative services such as maintenance of accounting records and investment of cash for all fund groups within the City. The various funds are charged for these services based on the City's indirect cost allocation plan. The overhead allocation paid to the General Fund of the City by the CWP was approximately \$1,679 and \$1,808 for the years ended June 30, 1998 and 1997, respectively, and is included in other operating expenses in the accompanying combined financial statements.

The City transferred \$4,707 and \$4,693 from its Debt Service Fund to the CWP during the years ended June 30, 1997 and 1996, respectively, to provide for general obligation bond debt service of the CWP.

The SFWD buys water from Hetchy. This amount, totaling \$19,037 for the years ended June 30, 1998 and 1997, respectively, has been included in operating transfers in the accompanying combined financial statements.

The CWP and SFWD buy electricity from Hetchy at market rates. These amounts, totaling \$10,032 and \$11,245 for the years ended June 30, 1998 and 1997, respectively, have been included in light, heat and power in the accompanying statements of operations.

- The CWP provides sewer services to other City departments at the nonresidential rates established by the Commission.
- The City's Department of Public Works provides certain engineering and other services to the Commission and charges amounts designed to recover that department's costs.

SFWD bills and collects sewer service charges on behalf of the CWP and charges amounts designed to recover that department's costs.

(12) Risk Management

The Commission is self-insured for general liabilities, property damage and workers' compensation claims. The risk of loss is managed internally by setting aside assets for claim settlement and recording a liability

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

representing an estimate of the cost of all outstanding claims and incurred but not reported claims. Claim liabilities are recorded when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount and, therefore, it is reasonably possible that claim liabilities could change in the future. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and legal factors. The liability is the best estimate of the Commission based on available information. Changes in the reported liability for the years ended June 30, 1998 and 1997 resulted from the following:

| | 1998 | 1997 |
|--|-----------|---------|
| Beginning of year liability | \$ 13,397 | 14,911 |
| Current year claims and changes in estimates | 3,810 | 663 |
| Current year claims payments | (1,393) | (2,177) |
| End of the year liability | \$ 15,814 | 13,397 |
| General liabilities and property damage | 12,503 | 10,424 |
| Workers' compensation | 3,311 | 2,973 |
| | \$ 15,814 | 13,397 |

(13) Commitments and Contingencies

Hetchy has contracted with Pacific Gas and Electric (PG&E) to provide Hetchy with backup power, services and transmission should Hetchy be unable to generate power sufficient to meet the minimum amounts of power guaranteed under certain long-term contracts. The PG&E agreement allows PG&E to review past billings paid by Hetchy and retroactively adjust these payments to actual backup power charges as finally determined by PG&E. During fiscal years 1998 and 1997, Hetchy purchased \$11,656 and \$11,258, respectively, of power, backup and transmission services.

In order to comply with Federal Energy Regulatory Commission regulations, Hetchy has contracted with the Modesto and Turlock Irrigation Districts to meet quality and depth of water standards on the Tuolumne River. Under this agreement, Hetchy is obligated to pay \$3,570 annually through 2001 for services rendered. In addition, Hetchy is required to pay 52% of environmental monitoring costs, not to exceed \$1,400, and to provide approximately \$750 over 20 years for habitat and facility improvements.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Notes to Combined Financial Statements

June 30, 1998

(with comparative information for June 30, 1997)

(dollars in thousands)

At June 30, 1998, the Commission has outstanding commitments with third parties of \$49,196 for various capital projects for materials and services.

(14) Subsequent Event

In June 1998, the voters passed Proposition H which effectively froze the water and sewer rates at their current levels until July 1, 2006, subject to certain exceptions. Due to the passage of Proposition H, Moody's Investor Services downgraded its rating of the Water bonds from Aa to A1 and of the Clean Water bonds from A1 to A2 in October 1998. In both cases, Moody's cited the lack of flexibility imposed by Proposition H and the inability to fund significant water improvements and significant sewer maintenance and/or meet new federal or state regulations that may arise during the Proposition H period.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combining Balance Sheet

June 30, 1998

(dollars in thousands)

| Assets | San Francisco Clean Water Program Fund Group | San Francisco Water Department | Hetch Hetchy Project | Combined Total |
|--|---|---|-------------------------------------|---------------------------|
| Current assets: | | | | |
| Deposits and investments with City Treasury | \$ 53,445 | 75,864 | 49,489 | 178,798 |
| Deposit and investments outside City Treasury | — | 51 | 339 | 390 |
| Receivables: | | | | |
| Water, power, and sewer, net | 27,506 | 9,325 | 7,755 | 44,586 |
| Interest and other | 1,123 | 1,262 | 4,218 | 6,603 |
| Total receivables | 28,629 | 10,587 | 11,973 | 51,189 |
| Materials and supplies—at average cost | — | 782 | 270 | 1,052 |
| Total current assets | 82,074 | 87,284 | 62,071 | 231,429 |
| Restricted assets: | | | | |
| Deposits and investments with City Treasury | 128,286 | 74,348 | — | 202,634 |
| Deposits and investments outside City Treasury | 37,726 | 9,151 | — | 46,877 |
| Interest receivable | 1,074 | 545 | — | 1,619 |
| Total restricted assets | 167,086 | 84,044 | — | 251,130 |
| Net property, plant and equipment | 1,393,561 | 409,295 | 203,148 | 2,006,004 |
| Bond issuance costs, net | 3,378 | 2,033 | — | 5,411 |
| Total assets | \$ 1,646,099 | 582,656 | 265,219 | 2,493,974 |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combining Balance Sheet

June 30, 1998

(dollars in thousands)

| Equity and Liabilities | San Francisco Clean Water Program Fund Group | San Francisco Water Department | Hetch Hetchy Project | Combined Total |
|--|---|--------------------------------------|----------------------------|-------------------|
| Current liabilities: | | | | |
| General obligation bonds, current portion | \$ 4,660 | 1,340 | — | 6,000 |
| Revenue bonds, current portion | 18,330 | 5,100 | — | 23,430 |
| State revolving loan funds, current portion | 10,904 | — | — | 10,904 |
| Accounts payable | 1,349 | 3,564 | 8,603 | 13,516 |
| Accrued payroll | 1,903 | 2,938 | 581 | 5,422 |
| Accrued vacation, sick leave, and workers' compensation, current payable | 1,225 | 3,544 | 1,232 | 6,001 |
| Bond interest payable | 10,129 | 2,349 | — | 12,478 |
| Suburban water rate agreement | — | 7,370 | — | 7,370 |
| Damage and claims liability, current payable | 6,418 | 3,260 | 245 | 9,923 |
| Deposits and construction advances | — | 980 | 176 | 1,156 |
| Other | — | 1,359 | 112 | 1,471 |
| Total current liabilities | 54,918 | 31,804 | 10,949 | 97,671 |
| Liabilities payable from restricted assets | 2,306 | 767 | — | 3,073 |
| Deferred revenue and other long-term liabilities: | | | | |
| Accrued vacation, sick leave, and workers' compensation | 1,024 | 4,355 | 1,354 | 6,733 |
| Damage and claims liability | — | 2,580 | — | 2,580 |
| Other | — | — | 150 | 150 |
| Deferred revenue | 5,422 | — | — | 5,422 |
| Total deferred revenue and other long-term liabilities | 6,446 | 6,935 | 1,504 | 14,885 |
| Long-term debt, less current portion: | | | | |
| General obligation bonds | — | 830 | — | 830 |
| Revenue bonds | 493,158 | 234,761 | — | 727,919 |
| State revolving loan funds | 167,700 | — | — | 167,700 |
| Total long-term debt | 660,858 | 235,591 | — | 896,449 |
| Total liabilities | 724,528 | 275,097 | 12,453 | 1,012,078 |
| Commitments and contingencies | | | | |
| Equity: | | | | |
| Contributed capital | 620,683 | 75 | — | 620,758 |
| Retained earnings—reserved for bond requirements and other commitments | 26,365 | 6,580 | — | 32,945 |
| Retained earnings—unreserved | 274,523 | 300,904 | 252,766 | 828,193 |
| Total equity | 921,571 | 307,559 | 252,766 | 1,481,896 |
| Total equity and liabilities | \$ 1,646,099 | 582,656 | 265,219 | 2,493,974 |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combining Statement of Income

For the year ended June 30, 1998

(dollars in thousands)

| | San Francisco Clean Water Program Fund Group | San Francisco Water Department | Hetch Hetchy Project | Combined Total |
|---|---|--------------------------------------|----------------------------|-------------------|
| Operating revenues: | | | | |
| Charges for services | \$ 140,898 | 121,137 | 81,667 | 343,702 |
| Rental income | — | 6,254 | 127 | 6,381 |
| Other revenue | — | 2,070 | — | 2,070 |
| Total operating revenues | 140,898 | 129,461 | 81,794 | 352,153 |
| Operating expenses: | | | | |
| Personal services | 27,356 | 48,645 | 12,291 | 88,292 |
| Contractual services | 5,808 | 3,342 | 22,681 | 31,831 |
| Light, heat and power | 6,396 | 3,636 | — | 10,032 |
| Materials and supplies | 6,056 | 4,812 | 947 | 11,815 |
| Depreciation and amortization | 39,990 | 20,437 | 8,131 | 68,558 |
| General and administrative | 675 | 4,949 | 6,297 | 11,921 |
| Services provided by other departments | 17,642 | 8,614 | 3,298 | 29,554 |
| Other | 2,919 | 8,077 | 10,061 | 21,057 |
| Total operating expenses | 106,842 | 102,512 | 63,706 | 273,060 |
| Operating income | 34,056 | 26,949 | 18,088 | 79,093 |
| Nonoperating revenues (expenses): | | | | |
| Operating grant – federal | 972 | 554 | 472 | 1,998 |
| Operating grant – state | 7,766 | — | — | 7,766 |
| Interest and investment income | 12,192 | 10,116 | 2,760 | 25,068 |
| Interest expense | (33,358) | (15,832) | — | (49,190) |
| Other, net | (4,356) | 5,011 | 144 | 799 |
| Net nonoperating (expenses) revenues | (16,784) | (151) | 3,376 | (13,559) |
| Income before operating transfers | 17,272 | 26,798 | 21,464 | 65,534 |
| Operating transfers: | | | | |
| Operating transfers in | — | — | 19,037 | 19,037 |
| Operating transfers out | — | (19,037) | — | (19,037) |
| Operating transfers from the City and County of San Francisco | 4,707 | 1,410 | — | 6,117 |
| Operating transfers to the City and County of San Francisco | — | (1,410) | (45,703) | (47,113) |
| Net operating transfers | 4,707 | (19,037) | (26,666) | (40,996) |
| Net income (loss) | \$ 21,979 | 7,761 | (5,202) | 24,538 |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combining Statement of Equity

For the year ended June 30, 1998

(dollars in thousands)

| | Contributed capital | | | Retained earnings | Total |
|---|------------------------|----------------------|--|-------------------|-----------|
| | Federal capital grants | State capital grants | Contribution from City and County of San Francisco | | |
| San Francisco Clean Water Program Fund Group: | | | | | |
| Equity at July 1, 1997 | \$ 464,678 | 71,918 | 108,238 | 265,028 | 909,862 |
| Net income | — | — | — | 21,979 | 21,979 |
| Federal and state capital grants | (8,381) | (1,889) | — | — | (10,270) |
| Allocation of depreciation | (11,975) | (1,906) | — | 13,881 | — |
| Balance at June 30, 1998 | 444,322 | 68,123 | 108,238 | 300,888 | 921,571 |
| San Francisco Water Department: | | | | | |
| Equity at July 1, 1997 | — | — | 75 | 299,723 | 299,798 |
| Net income | — | — | — | 7,761 | 7,761 |
| Balance at June 30, 1998 | — | — | 75 | 307,484 | 307,559 |
| Hetch Hetchy Project: | | | | | |
| Equity at July 1, 1997 | — | — | — | 257,968 | 257,968 |
| Net income | — | — | — | (5,202) | (5,202) |
| Balance at June 30, 1998 | — | — | — | 252,766 | 252,766 |
| Combined equity at June 30, 1998 | \$ 444,322 | 68,123 | 108,313 | 861,138 | 1,481,896 |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combining Statement of Cash Flows

For the year ended June 30, 1998

(dollars in thousands)

| | San Francisco Clean Water Program Fund Group | San Francisco Water Department | Hetch Hetchy Project | Combined Total |
|---|---|--------------------------------------|----------------------------|-------------------|
| Cash flows from operating activities: | | | | |
| Cash received from customers, including cash deposits | \$ 141,254 | 122,326 | 78,142 | 341,722 |
| Cash received from tenants for rent | — | 6,254 | 127 | 6,381 |
| Cash paid to employees for services | (26,966) | (47,943) | (12,036) | (86,945) |
| Cash paid to suppliers for goods and services | (11,630) | (19,009) | (28,968) | (59,607) |
| Cash paid for quasi-external transactions | (26,427) | (11,889) | (12,226) | (50,542) |
| Net cash provided by operating activities | 76,231 | 49,739 | 25,039 | 151,009 |
| Cash flows from noncapital financing activities: | | | | |
| Operating grants | 8,738 | 554 | 472 | 9,764 |
| Operating transfers in | — | 1,410 | 19,037 | 20,447 |
| Operating transfers out | — | (20,447) | (45,703) | (66,150) |
| Net cash provided by (used in) noncapital financing activities | 8,738 | (18,483) | (26,194) | (35,939) |
| Cash flows from capital and related financing activities: | | | | |
| Proceeds from sale of fixed assets | — | 2,537 | — | 2,537 |
| State revolving fund loan proceeds | 5,000 | — | — | 5,000 |
| Transfers from the City for debt service | 4,707 | — | — | 4,707 |
| Interest on long-term debt | (35,262) | (17,168) | — | (52,430) |
| Principal paid on long-term debt | (21,710) | (103,235) | — | (124,945) |
| Principal paid on loans | (10,317) | — | — | (10,317) |
| Acquisition and construction of capital assets | (27,706) | (25,899) | (4,797) | (58,402) |
| Payment of capital lease obligations | — | — | (51) | (51) |
| Other capital financing decreases | (1,182) | — | — | (1,182) |
| Net cash used in capital and related financing activities | (86,470) | (143,765) | (4,848) | (235,083) |
| Cash flows from investing activities: | | | | |
| Interest income received | 11,581 | 8,152 | 2,965 | 22,698 |
| Proceeds from sale of investments | 86,180 | 376,229 | — | 462,409 |
| Purchase of investments | (82,036) | (285,584) | — | (367,620) |
| Other investing activities | 1,354 | 2,941 | 145 | 4,440 |
| Net cash provided by investing activities | 17,079 | 101,738 | 3,110 | 121,927 |
| Increase (decrease) in cash and cash equivalents | 15,578 | (10,771) | (2,893) | 1,914 |
| Cash and cash equivalents: | | | | |
| Beginning of year | 161,447 | 145,359 | 52,721 | 359,527 |
| End of year | \$ 177,025 | 134,588 | 49,828 | 361,441 |

SAN FRANCISCO PUBLIC UTILITIES COMMISSION

Combining Statement of Cash Flows

For the year ended June 30, 1998

(dollars in thousands)

| | San Francisco Clean Water Program Fund Group | San Francisco Water Department | Hetch Hetchy Project | Combined Total |
|---|---|--------------------------------------|----------------------------|-------------------|
| Reconciliation of operating income to net cash provided by operating activities: | | | | |
| Operating income | \$ 34,056 | 26,949 | 18,088 | 79,093 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | | | |
| Depreciation and amortization | 39,990 | 20,437 | 8,131 | 68,558 |
| Provision for uncollectible accounts | 1,240 | — | — | 1,240 |
| Other | — | 3,260 | — | 3,260 |
| Changes in assets and liabilities: | | | | |
| Water, power, and sewer receivables, net | 356 | 1,922 | (3,462) | (1,184) |
| Due from other funds | 255 | — | 138 | 393 |
| Materials and supplies | — | 754 | (19) | 735 |
| Other receivables | 410 | 174 | (3,477) | (2,893) |
| Accounts payable | (189) | (1,452) | 5,264 | 3,623 |
| Accrued payroll | 66 | 552 | 84 | 702 |
| Accrued vacation, sick leave and workers' compensation | 47 | 339 | 355 | 741 |
| Due to other funds | — | (393) | — | (393) |
| Deferred credits and other liabilities | — | (2,803) | (63) | (2,866) |
| Net cash provided by operating activities | \$ 76,231 | 49,739 | 25,039 | 151,009 |
| Reconciliation of cash and cash equivalents to the balance sheet: | | | | |
| Deposits and investments with the City Treasury: | | | | |
| Unrestricted | \$ 53,445 | 75,864 | 49,489 | 178,798 |
| Restricted | 128,286 | 74,348 | — | 202,634 |
| Deposits and investments outside City Treasury | — | 51 | 339 | 390 |
| Total deposits and investments | 181,731 | 150,263 | 49,828 | 381,822 |
| Add: Restricted deposits outside City Treasury meeting the definition of cash equivalents | 796 | — | — | 796 |
| Less: Deposits and investments not meeting the definition of cash equivalents | (5,502) | (15,675) | — | (21,177) |
| Cash and cash equivalents at end of year on combined statements of cash flows | \$ 177,025 | 134,588 | 49,828 | 361,441 |
| Noncash investing, capital and financing activities: | | | | |
| Write-off of fixed assets | (15,296) | — | — | (15,296) |
| Depreciation on contributed capital | 13,881 | — | — | 13,881 |
| | \$ (1,415) | — | — | (1,415) |



SAN FRANCISCO PUBLIC UTILITIES COMMISSION



Annual Report 1998-1999

San Francisco, California
For the Year Ended June 30, 1999



SAN FRANCISCO PUBLIC UTILITIES COMMISSION
1155 MARKET ST., 4TH FLOOR, SAN FRANCISCO, CA 94103 • TEL. (415) 554-3155 • FAX (415) 554-3161



December 1, 1999

WILLIE L. BROWN, JR.
MAYOR

Honorable Willie L. Brown, Jr., Mayor

Honorable Board of Supervisors

COMMISSION

ANN MOLLER CAEN
PRESIDENT

FRANK L. COOK
VICE PRESIDENT

E. DENNIS NORMANDY
COMMISSIONER

VICTOR G. MAKRAS
COMMISSIONER

ANSON B. MORAN
GENERAL MANAGER

Dear Mayor Brown and Members of the Board:

In accordance with Section 4.103 of the Charter, I am pleased to forward the Annual Report for the Public Utilities Commission for Fiscal Year 1998-99.

During the year Hetch Hetchy Water & Power completed construction of two City-owned substations at San Francisco Airport and saved over \$4 million in capital costs. Construction was carried out at both the Water Treatment and Water Pollution control plants to improve operational efficiency without compromising delivery of water or treatment processes. The Land Management section continued to increase annual revenues through efficient and constant vigilance of the leasing process. Engineering continues for the much needed seismic upgrade to the Bay Division Pipelines and the improvement of water quality reliability and seismic upgrade to our water treatment plant in Sunol.

Finally, the Public Utilities Commission also transferred over \$39 million to the City's General Fund from dollars generated by Hetch Hetchy through the sale of surplus hydro power.

Sincerely,

Ann Moller Caen
President

DOCUMENTS DEPT.

MAY 11 2000

**SAN FRANCISCO
PUBLIC LIBRARY**

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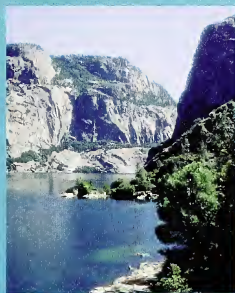
SAN FRANCISCO PUBLIC UTILITIES COMMISSION MISSION

To serve San Francisco and its Bay Area customers with reliable, high quality and affordable water, while maximizing benefits from power operations and responsibly managing the resources entrusted to its care.

To protect public health and the aquatic environment by providing safe, reliable and efficient collection, treatment and disposal of San Francisco's wastewater.

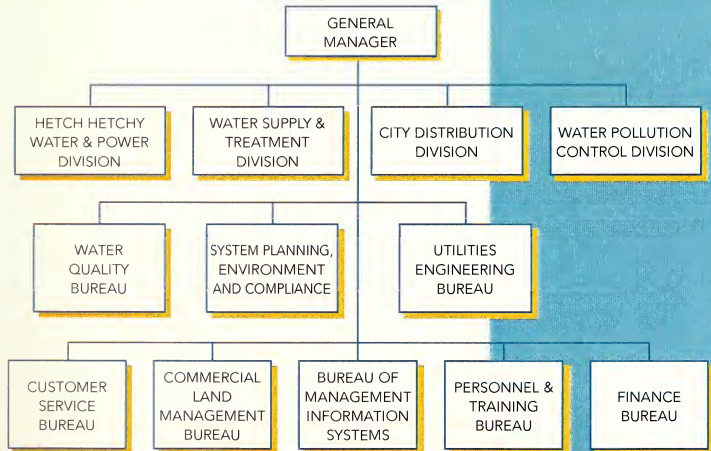
To conduct its business affairs in a manner that promotes efficiency, minimizes waste and assures rate-payer confidence.

To promote diversity and the health, safety and professional development of its employees.



Hetch Hetchy Reservoir near Yosemite provides water for 2.3 million people in the Bay Area.

Public Utilities Commission



INTRODUCTION

The San Francisco Public Utilities Commission ("SFPUC") oversees three of the City's municipal utilities:

- 1 The Hetch Hetchy project, which consists of water supply and power generating facilities in the Sierra Nevada;
- 2 The water treatment and distribution system, which delivers some of the purest drinking water in California to more than 2.3 million customers in the Bay Area; and
- 3 The wastewater treatment and disposal system, which collects and treats sewage and storm water flows within San Francisco.

Each of the three utilities represents a separate enterprise within the SFPUC which operates as a department of the City and County of San Francisco. Four divisions are responsible for the operation of the utilities – the Hetch Hetchy Water and Power Division, the Water Supply and Treatment Division, the City Distribution Division, and the Water Pollution Control Division. The SFPUC is governed by a five member Commission appointed for four year terms by the Mayor of San Francisco. The Commission appoints a General Manager who is responsible for day-to-day operations. Final budgetary authority is with the Mayor and the Board of Supervisors.

The SFPUC's utility system originates in the Sierra Nevada, where the *Hetch Hetchy Water and Power Division* maintains three reservoirs and more than 650 acres of watershed, much of which is located in Yosemite National Park. Water from the reservoirs is conveyed through a series of tunnels and pipelines from the mountains and across the Central Valley. En route, the water passes through four powerhouses, generating electricity for the City's municipal load and its other customers.

At Tesla Portal in the East Bay, the Hetch Hetchy water becomes the responsibility of the *Water Supply and Treatment Division*. The *Water Supply and Treatment Division* also draws another 15% of the total water supply from five reservoirs located in the East Bay and on the Peninsula. Water from these local sources is treated at two plants before it is delivered to City customers and 30 wholesale water surveyors in the San Francisco Bay Area.

At the City of San Francisco's border, the *City Distribution Division* assumes responsibility for storage and final delivery to San

Francisco customers. The Division maintains eleven reservoirs and eight storage tanks within the City, and uses a series of pump stations and more than 1,200 miles of water mains to reach every elevation and corner of the City.

Finally, the City's wastewater discharge and storm water runoff are captured by more than 900 miles of sewers and storm drains. The *Water Pollution Control Division* maintains the wastewater collection system and operates three treatment plants, where chemical and biological treatment

processes are used to remove pollutants before the wastewater is discharged into San Francisco Bay and the Pacific Ocean.

In addition to these four operating divisions, there are eight bureaus that provide technical and administrative support services. This approach eliminates duplication of effort and contributes to more efficient operations.

This annual report highlights the operations and accomplishments of the four divisions and eight bureaus. It also identifies some of the challenges that lie ahead for the SFPUC, including the implementation of a major capital improvement program and expansion into new service areas.

THE COMMISSION

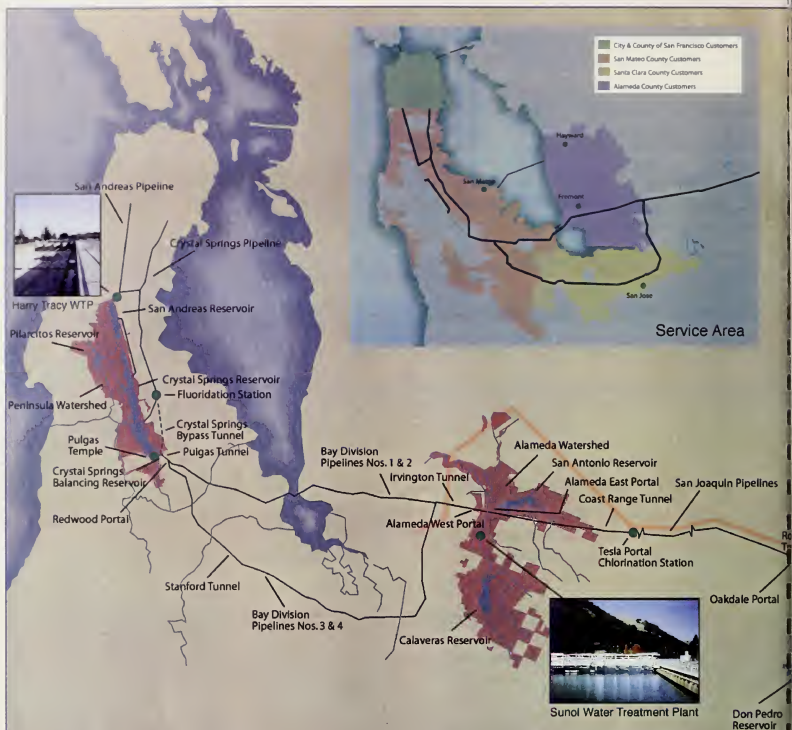
The SFPUC is led by five Commissioners, appointed by the Mayor who serve overlapping four-year terms. The Commission, in turn, elects one of its members to serve as its President each year. The Commission and the Mayor appoint the General Manager who serves as the chief administrative officer and is responsible for the SFPUC's day-to-day operations in accordance with the Commission's policies, the City Charter, and the Administrative Code. The General Manager appoints senior staff to run three utilities.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION MEMBERS DURING FY 1998-99

Ann Moller Caen, President
Frank L. Cook, Vice President
E. Dennis Normandy
Victor G. Makras

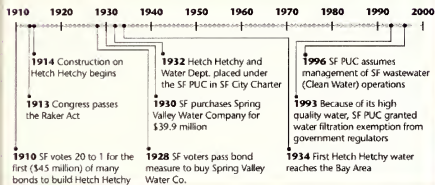


Secondary Clarifiers, Southeast Water Pollution Control Plant



San Francisco Public Utilities Commission System Map

Significant SF PUC Historical Dates



Holm Powerhouse



Hetch Hetchy

Cherry Power Tunnel

Hetch Hetchy Reservoir

Canyon Power Tunnel

Moccasin Reservoir

Priest Reservoir



Moccasin Powerhouse

HETCH HETCHY WATER AND POWER

*H*etch Hetchy Water and Power supplies more than 85% of the potable water delivered by the PUC. Water is collected in reservoirs in Yosemite National Park and delivered 165 miles to 2,300,000 users in San Francisco and the Bay Area. Electric power is generated through the Hetch Hetchy system's hydroelectric facilities when water is released from its reservoirs.

The Hetch Hetchy system is comprised of three principal reservoirs with a combined storage capacity of 660,000 acre-feet. In addition, Hetch Hetchy has rights to 570,000 acre-feet of storage in Don Pedro Reservoir, bringing total system capacity to 1.23 million acre-feet. The Hetch Hetchy system is renowned for its pristine supply – derived from snowmelt in the Sierras – and is one of only a very few sources of potable water in the United States that does not need to be filtered.

Hetch Hetchy's peak generation capacity is greater than 400 megawatts during the spring snow melt, when its reservoirs are full. Electricity is transported through Hetch Hetchy's transmission system to PG&E's Newark substation on the South Eastern shore of San Francisco Bay, where it is interconnected to the California electric grid. From there, Hetch Hetchy delivers its power to City facilities using PG&E's transmission and distribution system under a 30 year contract.

Hetch Hetchy supplies all of the electric power requirements of City municipal facilities, large and small, including City Hall, the municipal transit system, parks and recreational facilities, the Port of San Francisco, San Francisco International Airport, Moscone Center, Yerba Buena Gardens, water and sewer utilities, and street lighting. In addition, Hetch Hetchy supplies power to retail and wholesale customers, including the San Francisco Housing Authority, the San Francisco Redevelopment Agency, the San Francisco Unified School District, tenants at the Port and the Airport, the Modesto and Turlock Irrigation Districts, and other municipalities and special districts.

Hetch Hetchy's Bureau of Energy Conservation provides technical consultations to City policy makers, departments and Hetch Hetchy's retail customers for energy savings through a combination of policy initiatives, energy management, efficiency measures, load reduction and equipment retrofits. Hetch Hetchy's Bureau of Light, Heat and Power owns and maintains streetlights within the City. In addition, Hetch Hetchy provides cost-saving aggregation of wholesale natural gas supplies for City facilities.

HIGHLIGHTS FOR 1998-1999

Water Year – Over the past 12 months, the Hetch Hetchy Reservoir received 38 inches of precipitation. The spring snowmelt produced 667,000 acre-feet of water — approximately 1.8 times the



Moccasin Powerhouse

total capacity of the Hetch Hetchy Reservoir — over a four-month period. At Lakes Lloyd and Eleanor, snowmelt produced 354,000 acre-feet. Total precipitation and runoff for the year for both watersheds were about 110% of the long-term historic average. All reservoirs were full by late June.

Hetch Hetchy is an extremely profitable enterprise of the City. During FY 98/99, Hetch Hetchy returned nearly 2/3 of its net power revenues to the General Fund. When considered in conjunction with subsidies to General Fund Departments through discounted rates, the value of Hetch Hetchy's contribution to the City exceeded \$65 million during FY98/99.

The electric restructure has created significant financial pressure on Hetch Hetchy and the City, with electric revenues projected to decrease sharply over the next 2-3 years while both City and Hetch Hetchy costs are projected to increase. Throughout FY98/99, Hetch Hetchy's staff continued to work closely with the Commission to develop and implement a strategic business plan which would preserve or improve Hetch Hetchy's financial and market position in the newly competitive California electric market.

ELECTRIC BUSINESS ACTIVITIES

Electric Utility Deregulation – Hetch Hetchy continued to represent the City in proceedings before the Federal Energy Commission ("FERC"), the California Public Utilities Commission ("CPUC") and the state legislature relating to the California electric restructure. Although the electric restructure officially took effect in April 1998, risks remain high as the various stakeholders attempt to improve their relative market and financial positions at the expense of others through promulgation of the thousands of detailed rules and procedures which will implement the principles of the restructured market.

Presently, in addition to protecting the City, the City's residents and businesses, and Hetch Hetchy from adverse impacts of the California electric restructure, Hetch Hetchy is working diligently to strengthen the City's electric system. The PG&E outage of December 8, 1998 demonstrated the City's vulnerability to extended outages when the single transmission corridor serving the City is taken out of service. This event was followed an explosion at PG&E's aged Hunter's Point Power Plant on July 12, 1999 which took the largest generation unit out of service for an extended period of time. Loss of Hunter's Point Unit #4 has reduced the amount of available in-City generation below that needed to serve the City's loads in case of the loss of another generation or transmission facility. Hetch Hetchy is the City's technical expert in discussions among PG&E, the ISO and other stakeholders to identify and implement effective near-term solutions for reducing the City's vulnerability to power outages, as well as to increase the City's electric service reliability overall.

The issues associated with improving the City's electric reliability are directly linked to the shutdown of the Hunter's Point Power Plant.

Powerhouses/Maximum Capacity (Megawatts)

| | |
|------------------|---------------|
| Holm | 165 MW |
| Kirkwood | 122 MW |
| Moccasin | 115 MW |
| Moccasin Lowhead | 3 MW |
| | 405 MW |

Specifically, since the Hunter's Point Power Plant is currently needed to maintain system reliability, it cannot be shut down until some suitable combination of new capacity for transmission, generation or energy conservation is in place. In order to assure the earliest practical implementation of the agreement to shut down this old, polluting plant while still protecting electric reliability, Hetch Hetchy, the City's technical expert, has taken a lead role in working with the parties to facilitate the development and implementation of solutions to these problems.

Airport – Hetch Hetchy completed construction of two City owned substations at the San Francisco International Airport to support the Airport expansion. Hetch Hetchy's redesign of these substations saved the City more than \$4 million in capital costs.

Treasure Island - Hetch Hetchy continued to manage the operations and maintenance of multi-utilities (electric, gas, water and sewer) services at Treasure and Yerba Buena Islands under a "Cooperative Agreement" between the Navy and the City. During FY98/99, Hetch Hetchy assisted the Mayor's Project Office in all utilities matters associated with readying vacant properties for lease, including the lease of residential units. In addition, Hetch Hetchy continues to assist the City's Treasure Island Development Authority in long term infrastructure planning and preparation for the eventual transfer of Treasure Island from the Navy to the City.

Hunter's Point Naval Shipyard – Hetch Hetchy is leading a PUC team in discussions with the selected developer of the Hunter's Point Naval Shipyard. In addition to providing assistance to the City in development of a "Project Development Concept" and negotiation of a development contract, the scope of the PUC's participation includes technical review and analysis of the developer's proposed interim and long-term infrastructure plans.

Renewables – Hetch Hetchy has secured a \$1.5 Million subsidy from the California energy Commission towards continued design and development of two renewable energy projects – a 2 megawatt digester gas co-generation project at the City's Southeast Treatment Plant and a 1 megawatt conduit hydroelectric plant at the City's Sunol Filtration Plant. In addition, Hetch Hetchy commenced an effort to identify other opportunities for development of renewable resources.

LOOKING FORWARD

In the coming year Hetchy will be working with the Commission to finalize and implement its business plan. Within our Moccasin operations, we will be letting contracts to move forward long stalled capital projects. In addition we will be seeking partners to install the latest forms of distributed generation and energy conservation features in the building. Hetchy will continue to take the lead for the City in working with regulators, developers, and the citizens around the issues related to the shut down and replacement of the Hunters Point power plant.



Bay Division Pipelines

WATER SUPPLY AND TREATMENT DIVISION

Hetch Hetchy Water and Power maintains control of the water system until it reaches Alameda County. The Water Supply and Treatment Division then assumes control. The water is conveyed through four pipelines to customers located in Alameda, Santa Clara and San Mateo counties, as well as San Francisco. The Division provides another 15% of the total water supply from reservoirs located in the East Bay and on the Peninsula. These local water sources require filtration and treatment at two plants. In 1997-98, the Water Supply and Treatment Division delivered on average 250 million gallons per day (mgd) to customers throughout the service area.

HIGHLIGHTS FOR 1997-1998

The Division conducted a number of activities in three major areas in the course of the year. The most significant accomplishments are summarized below:

Land and Resource Management

- Completed the draft Watershed Management Plans, with the draft Environmental Impact Report underway.
- Completed mitigation measures associated with the Calaveras pipeline project.
- Started the Right-of-Way Management Planning effort under the direction of the Division's new Right-of-Way Manager.
- Initiated biological studies and assessments in relation to the Bay Area Trail and the Alameda Fisheries Restoration Program.
- Using the Conservation Corps, accomplished fire hazard reduction work (vegetation management) in watershed lands.

Facility Improvements

- Placed in service a new reservoir, along with replacement of one



Sunol Water Treatment Plant

- supply well pump for the Castlewood service.
- Removed and replaced filter media in four filter beds at the Harry Tracy Water Treatment Plant.
- Increased liquid oxygen storage for ozone production by over 200% at the Harry Tracy Water Treatment Plant.
- Upgraded the chemical storage and feed system to enhance safety, reliability and process at the Harry Tracy Water Treatment Plant.
- Constructed and placed in operation a new chemical feed station for non-ionic polymer, for the purpose of enhanced coagulation at the Sunol Water Treatment Plant.
- Designed and installed new baffling in the waste wash water recovery ponds to improve the quality of wash water being recycled back into the plant at the Sunol Water Treatment Plant.
- Obtained the Phase III Partnership for Safe Drinking Water Award at the Sunol Valley Water Treatment Plant which was one of the first such plants to receive this award.

Operations Planning

- Efforts are underway in the development of a comprehensive preventive maintenance program to include all facilities and equipment within the division.
- In conjunction with the Bay Area Water Users Association, revisions and improvements are being made to the Emergency Operations and Notification Plan.

LOOKING FORWARD

In the coming year, the Water Supply and Treatment Division will continue the initiatives started in 1997- 1998 as well as several new efforts.

- A Division-level emergency response plan is being developed and staff will be trained on use of the plan.
- A fire incident reporting and data collection process will be developed for Land Resources Management.
- Increased construction activities at the two treatment plants must be managed while maintaining water treatment and delivery capabilities.
- Phased implementation on recommendations made by the Productivity Task Force on scheduling, cross-training, information management, preventive maintenance and supervision.
- Provide a database to show Land Engineering permits on-line. This would allow instant access for all interested parties within the PUC to view the status of permits under review by the Land Engineering Section and all the permits which have been approved.

CITY DISTRIBUTION DIVISION

The City Distribution Division stores, distributes, and delivers water directly to customers in San Francisco. The Division maintains the water distribution system within the City, which consists of reservoirs and auxiliary tanks, pumping stations and a network of approximately 1,250 miles of pipelines. On average, the Division delivers approximately 80 million gallons of water a day to nearly 770,000 people within the City.

The City Distribution Division conducts a range of services:

- Provides 24 hour-a-day response capability for water main breaks and for pumping, pressurizing and disinfection of the water distribution system.
- Provides information on the in-City water distribution system to utilities, developers, owners and the general public. Responds to all multiple alarm fires to assure sufficient water pressure and supply for fire suppression.
- Operates and maintains 18 pumping stations supplying 18 reservoirs, and storage tanks.

San Francisco Water Distribution System Components

8 storage tanks
10 pump stations
11 reservoirs
440 million gallons storage capacity
1,250 miles of pipeline
15,000 distribution valves
167,000 metered services



Reservoirs and pumping stations in San Francisco. The water system in San Francisco consists of over 1,200 miles of pipe, the distance between San Francisco and Denver.

Storage Capacity of In-City Reservoirs

(millions of gallons)

| | |
|--------------------------|--------------|
| <i>Albion</i> | <i>176.7</i> |
| <i>University Avenue</i> | <i>140.9</i> |
| <i>Alamo</i> | <i>31.4</i> |
| <i>Summit</i> | <i>14.0</i> |
| <i>College Hill</i> | <i>13.5</i> |
| <i>Stanford Heights</i> | <i>12.9</i> |
| <i>Merced Manor</i> | <i>9.5</i> |
| <i>Lombard</i> | <i>2.7</i> |
| <i>Hunter's Point</i> | <i>1.1</i> |
| <i>Potrero Heights</i> | <i>1.0</i> |

- Maintains, repairs and upgrades as necessary 1,250 miles of water mains.
- Protects and coordinates work done by others to assure that San Francisco Water Department facilities are not damaged or destroyed.
- Installs, repairs and maintains services connecting individual customers to water mains.
- Identifies and repairs underground leaks.
- Performs landscape maintenance of 984 acres of Division land, including right-of-ways, reservoirs, open space and parks.

HIGHLIGHTS FOR 1997-1998

Water Main Repair and Replacement – As part of the continuous water main repair and replacement program, the Division replaced 30,700 linear feet of water mains.

The Division also made the following types of repairs:

| | |
|---------------------------------|------|
| Main breaks | 106 |
| Connections | 125 |
| Main extensions and relocations | 2/13 |
| Steel main leaks | 1 |
| Cut in new gate services | 5 |

Service Renewals – Water services connect individual customers with the City's water mains. The Division is responsible for connecting new customers, maintaining and replacing deteriorated services and installing new meters:

| | |
|---------------------|-------|
| New services | 586 |
| Service renewals | 898 |
| Meter installations | 4,841 |
| Service Maintenance | 573 |

Meter Replacement – The Division has an ongoing program to monitor and replace the more than 167,000 meters that measure the amount of water delivered to each customer. Accurate meters help ensure that customers are billed properly for their water consumption. This year's meter replacement activities included:

| | | | |
|--------|-------|---------------|-------|
| Set | 759 | Scrap | 5,285 |
| Change | 5,415 | Special test | 790 |
| Repair | 308 | Field repairs | 3,192 |
| Home | 234 | Shop changes | 375 |

Treasure Island – In April 1997, the Navy contracted with the City to maintain and operate the water distribution system serving Treasure Island and Yerba Buena Island. The system, which consists of four reservoirs and four pump stations as well as water mains and connections, is old and in disrepair and lacks modern controls. The City Distribution Division is working with Treasure Island representatives to maintain the water system.

LOOKING FORWARD

The Division working with the Utilities Engineering Bureau and Water Quality Bureau intends to continue much needed repairs to reservoirs, pump stations, storage tanks and other facilities that are reaching or have exceeded their life expectancy.

WATER POLLUTION CONTROL DIVISION

Water Pollution Control operates and maintains the City's water pollution control system. The system is made up of collection sewers, transport and storage boxes, pump stations, overflow structures, treatment plants and outfalls. The Division's mandate is to maximize treatment and minimize combined sewage overflow, as dictated by the discharge permits issued by the State regulatory authority.

San Francisco has a combined sewer system in which both domestic and commercial/industrial sewage as well as storm water runoff are collected in the same sewer. As a result, the system captures and treats more wastewater to a higher level of treatment than nearly any other system in the greater Bay Area. During dry weather, the system collects, treats and discharges up to 90 million gallons of sewage a day. When it rains, the system may collect and treat as much as 465 million gallons of combined sewage and storm water a day.

HIGHLIGHTS FROM 1997-1998

Within the City proper, Water Pollution Control is responsible for maintaining more than 900 miles of sewers, operating 20 pumping stations and three wastewater treatment plants, identifying and implementing system repairs and improvements and planning for future operations. In addition, WPCD operates and maintains the wastewater collection and treatment system on Treasure Island under contract with the U. S. Navy. Significant achievements in 1998-99 were:

North Point Plant Improvements – The Phase 3A contract was completed, the third of several phases of improvements to the North Point Plant. When the remaining phases are completed these improvements will upgrade and renovate this wet weather facility consolidating the treatment processes at the facility and improving the energy and operational efficiency of the plant.

Southeast Plant – The plant received a Silver Award for excellent compliance with discharge permit conditions from the Association of Metropolitan Sewerage Agencies (AMSA) for the fourth consecutive year. The Distributed Control

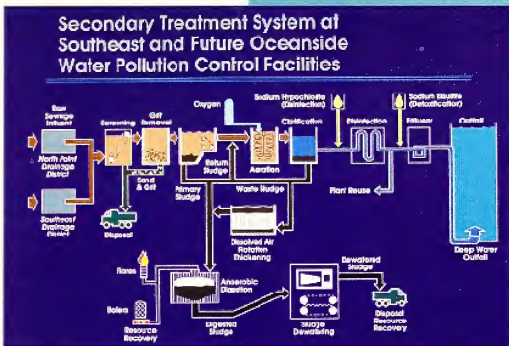
System was upgraded for Y2K compliance. The second year of a



A schematic map of the wastewater system.

two-year contract to repair the aging and corroding aeration process facility is being completed. Another contract replaced the failing launders in the seven primary tanks and also repaired concrete corrosion in the tanks. The Custer and Davidson Street area did not suffer any flooding as a result of the successful emergency contract work done last summer.

Oceanside Plant - The plant received a Gold Award for excellent compliance with discharge permit conditions from the Association of Metropolitan Sewerage Agencies (AMSA) for the fourth consecutive year. Single-compressor operation of the oxygen generating facility has proven successful. We have realized substantial power cost savings while continuing to meet biological treatment system demand. Odor abatement at 24th Avenue and West Clay Street was completed with improvements to the odor control system that serves the area.



Treasure Island - The Division continued operation of the wastewater system on Treasure Island, which also serves Yerba Buena Island, on a contract basis with the Navy. The existing effluent disinfection system was modified to replace the use of gaseous chlorine with liquid sodium hypochlorite. This provides a safer work environment for our employees and our neighbors while at the same time providing efficient and reliable disinfection of the plant effluent.

LOOKING FORWARD

In the coming year, the Division intends to continue to place emphasis on the maintenance and repair of the sewage collection system. We expect to implement the new GIS database which will enhance our ability to track field maintenance activities. Among other things this will improve our ability to respond to customer questions in a timely and accurate manner.

In addition, the Division will replace its existing computerized maintenance management system, called ELKE, with new software called MAXIMO. This will not only improve our ability to track maintenance activities with more precision, but will also provide a much more user friendly interface so that we can continue in our efforts to reduce the amount of paper documents that need to be generated.

SFPUC BUREAUS

The four operating divisions receive technical and administrative support from eight service bureaus. This approach eliminates duplication of efforts and contributes to more efficient operations. Several functions have been reassigned among the bureaus to improve services to the operating divisions and, ultimately, to customers.

UTILITIES ENGINEERING BUREAU

The Utilities Engineering Bureau provides engineering, construction management, and contracting services for the water, power and clean water capital improvement programs of the SFPUC. UEB assesses the condition of storage, transmission and treatment facilities, and recommends necessary repairs or upgrades. It designs the facility improvements to meet operating needs within budget and scheduled constraints. UEB then manages the construction of facilities and implements necessary upgrades and repairs. In 1998-99, UEB was responsible for \$172 million in capital improvements to water and power facilities.

HIGHLIGHTS FROM 1998-1999

- Completed preliminary engineering of \$6 million in seismic upgrades of Bay Division Pipelines #1 and #2 crossing the Hayward Fault. The seismic upgrades will improve the survivability of the pipelines during a major earthquake by repairing deteriorated trestle components supporting these pipelines in the West Bay.
- Completed preliminary engineering of \$35 million project to improve water quality reliability and seismically upgrade the Sunol Valley Treatment Plant. These improvements will help to increase capacity to about 150 mgd in direct filtration mode, and 120 mgd in conventional treatment mode for the Sunol Treatment Plant.
- Replaced the sluice gates which control the flow from Moccasin Reservoir into the Foothill Tunnel. New sluice gates and hydraulic controls were installed, along with some concrete replacement at the Moccasin Powerhouse, for a total cost of \$720,000.



- Modified the piping and valving at San Antonio Pump Station to increase the flexibility of operations and maintenance. With the \$1.5 million in modifications to the piping and valves, it will be possible to keep a minimum of 3 pumps in operation while maintenance is performed on any one pump.
- Reacting to an emergency landslide at Polhemus, UEB evaluated the impacts of the landslide on the existing water pipes, and designed and constructed protective measures for a total cost of approximately \$2.6 million.
- Replaced Castlewood Reservoir at a cost of about \$1.7 million. The existing 240,000 gallon reservoir was cited by the State Department of Health Services for multiple violations which required the replacement and repair of major sections of the reservoir.
- Completed re-roofing of six structures within San Francisco's City Distribution Division yard, for a cost of about \$1.1 million.
- Completed conceptual engineering and design documents for the Sunol Temple Restoration project for a cost of \$2 million through construction.
- Completed construction documents for the installation of a SCADA system for the Water Department facilities with a \$20 million cost through construction.
- Repaired and replaced numerous road sections, slides and other facilities for Hetch Hetchy caused by El Nino at a cost of \$7.5 million.
- Made repairs to Hetch Hetchy mountain tunnel adits at a cost of \$873,000.
- Replaced approximately six miles of structurally and hydraulically inadequate sewers within the City at a cost of approximately \$10 million under the Clean Water Repair and Replacement Program.
- Initiated the construction phase of the South East Water Pollution Control Plant Improvements to upgrade plant capacity to 250 million gallons per day.
- Installed approximately 13 miles of large diameter ductile iron pipe at a cost of about \$8.8 million for conveying potable water within the City's Distribution system.



FINANCE

The Bureau of Finance provides financial support and direction to the divisions and bureaus of the SFPUC. The Bureau's functions include: Development, preparation, and monitoring of annual operating and capital budgets; preparation of monthly reports and annual financial statements; development of projections of water and sewer revenues; development and implementation of short and long term debt program; internal audits; and determination of wholesale and retail water and sewer rates.

HIGHLIGHTS FROM 1998-1999

- Responsible for the first year completion of separate financial statements for Hetch Hetchy Water and Power for fiscal year ending 6/30/99. (Prior years' financial statements were presented jointly with the Water Department.)
- Completed the year-end financial audit on schedule.
- Successfully trained four accounting interns assigned through the Controller's Office citywide departmental training program. The four received promotions to senior accountants in other departments based on Accounting's training efforts.
- Established new internal audits program and completed first compliance audit of a PUC contractor.
- Received all local and state approvals to accept a \$50 million revolving fund loan to defease outstanding debt of the Clean Water Enterprise.
- Developed a budget and financial plan necessary to accommodate the expansion of the General Engineering Division as part of the expanded capital improvement program for the PUC.
- Developed and implemented spending plans for operating and capital budgets.
- Developed capital projects tracking reports for Water and Hetch Hetchy.
- Provide alternative funding for Water Capital Improvement Program due to rescheduling debt issuance (i.e. originally set for issuance in 1998).

BUREAU OF MANAGEMENT INFORMATION SYSTEMS

The Bureau of Management Information Systems (BMIS) provides data processing, computer systems development and office automation services to all SFPUC divisions and bureaus. The Bureau maintains and improves computer systems for processing water and sewer billing data, facilities maintenance data, and payroll

and other financial data. To support these and other functions, the Bureau also maintains a computer network of more than 1000 microcomputers, which are installed throughout various SFPUC locations.

HIGHLIGHTS FROM 1998-1999

In 1998-1999 the Bureau made the following improvements in the SFPUC computerized systems:

- Replaced hard copy financial and personnel vacancy reports with more timely and efficient Intranet access to this data.
- Implemented new customer payment options including automatic payment of bills directly from customer's checking accounts and credit card payments by phone using an interactive voice response system.
- Installed 300 networked computers for increased personal efficiency and improved data sharing among the various organizational units.

PERSONNEL AND TRAINING

The Bureau of Personnel and Training provides services related to human resource and payroll management, and acts as the liaison with the Department of Human resources, the Civil Service Commission, and the Controller's Payroll Services Division. The Bureau functions include: classification, examination, payroll position control, labor relations, disciplinary matters, affirmative action and equal opportunity compliance, training and general personnel administration. The 1998 – 1999 year presented tremendous challenges in the Bureau in its efforts to keep up with the growth of the PUC.

HIGHLIGHTS FROM 1998-1999

- Concluded Celebrating Diversity training for all PUC employees. Developed and began delivered training to all employees in Prevention of Sexual Harassment and Gender at Work.
- Developed an automated reporting system to track requisition processing and report on current vacancies. Put the reports online thereby making them routinely available to managers on the Intranet and eliminating paper distribution.
- Established a new series of classifications – Program Manager I, II, & III Classified 150 positions
- Administered 24 examinations
- Filled 404 positions

The Water Quality Bureau (WQB) ensures that the SFPUC complies with all current and future water quality regulations, including the Federal Safe Drinking Water Act, the California Code of Regulations Titles 17 and 22, San Francisco Ordinance 84-356 (Cross Connection Control), and sections of the Federal Clean Water Act. WQB assures compliance through sampling and analysis, process engineering, applied research and data review, field inspections, cross connection control program management, field project oversight, regulatory liaison, hazardous materials management, and laboratory testing. WQB also responds to all customer complaints and inquiries, and posts beach safety warnings after sewage overflows.

HIGHLIGHTS FROM 1998-1999

- Collected over 100,000 drinking water and wastewater samples in the service area stretching from Yosemite National Park to the Pacific Ocean.
- Conducted over 500,000 analytical (i.e., chemical, microbiological, biological, and physical) tests on drinking water and wastewater samples.
- Processed 6,338 backflow prevention device tests and inspected 540 new backflow device installations to prevent contamination of drinking water with unsanitary sources. Continued program to assess potential for contamination of the potable water distribution system from the Fire Department's high pressure Auxiliary Water Supply System.
- Completed the final six months of monitoring required under the USEPA mandated Information Collection Rule ICR, a nationwide data gathering project designed to assist in the formulation of new regulations related to microbiological contaminants and disinfection byproducts. Initiated additional volunteer testing under the ICR Supplemental Survey, a one-year program for the nation's largest utilities.
- Responded to more than 393 consumer complaints within four hours of initial contact.
- Established satellite labs at the Sunol Valley Water Treatment Plant (SVWTP), Harry Tracy Water Treatment Plant (HTWTP), and Moccasin to conduct regulatory and process control monitoring.
- Developed comprehensive water quality event response guidelines and a detailed procedure for public notification and customer communication.
- Conducted a regulatory monitoring program for lead and copper at approximately 3,000 customers taps throughout the entire SFPUC regional water system service area.



- Performed a source water treatability study to identify strategies to improve treatment at HTWTP during challenging winter conditions.
- Conducted an evaluation of the City chlorine feed facilities and prepared recommendations to improve safety, reliability, and operation of the systems.
- Provided project engineering services for the \$20.5 million upgrade of the SVWTP.
- Performed field investigation and inspection of potential sources of contamination in the Hetch Hetchy, Lake Eleanor, Cherry Lake, Early Intake, Priest Reservoir, and Moccasin Watersheds.



CUSTOMER SERVICE

The Customer Service Bureau is the primary point of contact with the SFPUC for water and sewer customers. The Bureau maintains 144,381 residential accounts and 22,944 commercial and municipal accounts in San Francisco. It provides for billing and collection of water and sewer charges, administration of customer accounts (including opening and closing accounts), installation of new services, meter reading, and field services such as inspections. The Bureau oversees the ultra-low flow toilet rebate and give-away programs and administers a water conservation "best management practices" program.

The Bureau is also responsible for the development of public information programs for water and sewer construction projects, and serves as an administrative source for water and sewer complaints.

Among its public information functions is the administration of the SFPUC speaker's bureau and the preparation of publications, such as the semi-annual *Water Quality Report* and billing inserts.

HIGHLIGHTS FROM 1998-1999

- Initiated payment options that allow customers over the phone payment by credit card and bill payments by automatic deduction from a customer's checking account.
- Entered into a Memorandum of Understanding with the Tax Collector's Bureau of Delinquent Revenue to collect delinquent closed account.
- Contracted with the Treasurer's Office to process daily water and sewer bill payments.
- Completed a Business Recovery Plan that allows normal business operations to restart after a disaster.
- Developed a process to identify unmetered water accounts that allows for the collection of unpaid back charges.

- Continued a program of reevaluating the accuracy of flow factors (a variable that determine the amount of water not returned to the sewer system) for over 2,600 accounts.
- Published the first ever Environmental Protection Agency mandated Consumer Confidence Report and mailed to 327,000 residences and businesses in San Francisco.
- Distributed 12,000 ultra-low flow flush toilets to the general public at 10 Citywide sales events, with one sale incorporating an Environmental Fair and a second, a children's costume contest to raise food for a local Food Bank.
- Won the California Water Awareness Campaign's Water Efficiency Award for Residential Programs.
- Provide public outreach on over two dozen water and sewer related construction projects both inside and outside of San Francisco.
- Continued various High School Outreach Programs that employed students to work in various student assistant capacities throughout the Public Utilities Commission.
- Initiated tours (advertised in the Water Billing Insert Program) of major Public Utilities Commission facilities both in and outside of San Francisco, including a Water Treatment Plant and two Water Pollution Control Treatment Plants.
- Spear-headed the Public Utilities Commission- wide Combined Charities Campaign that resulted in the highest ever PUC contribution total and ranked second in the entire City government giving effort.

COMMERCIAL LAND MANAGEMENT

The Bureau of Commercial Land Management manages the SFPUC's commercial interest in lands and properties owned by the SFPUC. The Bureau monitors lease and permit negotiations, insurance renewals, delinquent rent collections, property taxes and assessments, and land sales and purchases. Its staff also recommends policies to the SFPUC and implements procedures approved by the SFPUC relating to land use, rental, management, and disposal of properties under its control. The Bureau seeks to identify means of increasing revenues by developing innovative uses of pipeline rights-of-way, treatment facilities, and watershed properties in a manner consistent with the goals of the SFPUC.

HIGHLIGHTS FROM 1998-1999

- Increased annual rent revenues by approximately 1 million dollars.
- Negotiated approximately 30 new leases and permits.

BUREAU OF SYSTEM PLANNING, ENVIRONMENT AND COMPLIANCE

The Bureau of System Planning, Environment and Compliance is responsible for:

- Planning for the continued service of reliable high quality water to San Francisco and its customers, and the continued collection, treatment and disposal of wastewater for San Francisco in compliance with current and anticipated laws and regulations.
- Protecting the environment, our citizens, employees and facilities by regulating industrial waste discharges to the sewerage system and implementing the sewer user charge program.
- Assisting the PUC in complying with and implementing environmental and regulatory compliance efforts.

The Bureau is a merger of the Bureau of Environmental Regulation and Management and System Planning and Regulatory Compliance.

HIGHLIGHTS FROM 1998-1999

- In 1998-99, the System Planning Bureau undertook the preparation of Capital program priorities for each of the SFPUC enterprises – Water, Clean Water and Hetch Hetchy. The purpose of these reports was to prioritize the Capital Improvement needs of each operating division, based on input from staff and managers of the operating divisions, Utilities Engineering Bureau and Water Quality Bureau. An implementation plan and schedule of funding required to support the overall SFPUC capital program is currently being prepared.
- Received the Public Education Award from the Association of Metropolitan Sewage Agencies (AMSA) for developing and implementing the less toxic pest control program.
- Identified and verified all commercial stormwater sources in the City.
- Successfully assisted all PUC facilities in complying with the underground storage tank regulations and requirements.
- Completed conceptual engineering for the conversion of the Hetch Hetchy water treatment to chloramine.
- Sunol Filter Plant conceptual engineering for near term improvements were nearly completed and capacity upgrades concept was approved by the SF PUC.



Industrial Waste Inspector: San Francisco has pretreatment standards which prevent industries from discharging harmful amounts of wastes to sewers.



HETCH HETCHY WATER AND POWER

Financial Statements

June 30, 1999 and 1998

(With Independent Auditors' Report Thereon)

HETCH HETCHY WATER AND POWER

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Three Embarcadero Center
San Francisco, CA 94111

Independent Auditors' Report

Honorable Mayor and Board of Supervisors
City and County of San Francisco, California:

We have audited the accompanying financial statements of Hetch Hetchy Water and Power (Hetch Hetchy) of the City and County of San Francisco, California (the City), as of and for the year ended June 30, 1999, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 1, the financial statements present only Hetch Hetchy and are not intended to present fairly the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hetch Hetchy Water and Power of the City and County of San Francisco, California, as of June 30, 1999, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

The Year 2000 supplementary information on pages 14 and 15 is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board, and we did not audit and do not express an opinion on such information. Further, we were unable to apply to the information certain procedures prescribed by professional standards because of the nature of the subject matter underlying the disclosure requirements and because sufficiently specific criteria regarding the matters to be disclosed have not been established. In addition, we do not provide assurance that Hetch Hetchy is or will become Year 2000 compliant, that Hetch Hetchy's Year 2000 remediation efforts will be successful in whole or in part, or that parties with which Hetch Hetchy does business are or will become Year 2000 compliant.

KPMG LLP

October 22, 1999



KPMG LLP, KPMG LLP, a U.S. limited liability partnership, is a member of KPMG International, a Swiss association.

HETCH HETCHY WATER AND POWER

Balance Sheets

June 30, 1999

(with comparative amounts for June 30, 1998)

(dollars in thousands)

| Assets | 1999 | 1998 |
|--|------------|---------|
| Current assets: | | |
| Deposits and investments with City Treasury | \$ 56,390 | 49,489 |
| Deposits and investments outside City Treasury | 14 | 339 |
| Receivables: | | |
| Charges for services | 8,769 | 7,755 |
| Due from the City and County of San Francisco | 4,745 | 1,744 |
| Interest and other | 1,295 | 2,474 |
| Total receivables | 14,809 | 11,973 |
| Materials and supplies – at average cost | 292 | 270 |
| Total current assets | 71,505 | 62,071 |
| Net property, plant, and equipment | 203,240 | 203,148 |
| Total assets | \$ 274,745 | 265,219 |
| Liabilities and Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 11,044 | 8,603 |
| Accrued payroll | 661 | 581 |
| Accrued vacation, sick leave, and workers' compensation, current payable | 1,295 | 1,232 |
| Damage and claims liability, current payable | 317 | 245 |
| Deposits, advances and other liabilities | 201 | 288 |
| Total current liabilities | 13,518 | 10,949 |
| Long-term liabilities: | | |
| Accrued vacation, sick leave, and workers' compensation | 1,738 | 1,354 |
| Damage and claims liability | 2,013 | — |
| Other | 93 | 150 |
| Total long-term liabilities | 3,844 | 1,504 |
| Total liabilities | 17,362 | 12,453 |
| Equity: | | |
| Contributed capital | 1,661 | — |
| Retained earnings – unreserved | 255,722 | 252,766 |
| Total equity | 257,383 | 252,766 |
| Total liabilities and equity | \$ 274,745 | 265,219 |

See accompanying notes to financial statements.

HETCH HETCHY WATER AND POWER

Statements of Revenues, Expenses and Changes in Retained Earnings

Year ended June 30, 1999

(with comparative amounts for June 30, 1998)

(dollars in thousands)

| | <u>1999</u> | <u>1998</u> |
|---|-------------------|-----------------|
| Operating revenues: | | |
| Charges for services | \$ 86,670 | 81,667 |
| Rental income | <u>150</u> | <u>127</u> |
| Total operating revenues | <u>86,820</u> | <u>81,794</u> |
| Operating expenses: | | |
| Personal services | 11,048 | 10,614 |
| Contractual services | 23,664 | 22,681 |
| Materials and supplies | 1,460 | 947 |
| Depreciation and amortization | 8,383 | 8,131 |
| General and administrative | 13,993 | 9,115 |
| Services provided by other departments | 1,478 | 2,157 |
| Other | <u>2,764</u> | <u>10,061</u> |
| Total operating expenses | <u>62,790</u> | <u>63,706</u> |
| Operating income | <u>24,030</u> | <u>18,088</u> |
| Nonoperating revenues: | | |
| Operating grant – federal | 244 | 472 |
| Interest and investment income | 2,173 | 2,760 |
| Other, net | <u>175</u> | <u>144</u> |
| Total nonoperating revenues | <u>2,592</u> | <u>3,376</u> |
| Income before operating transfers | <u>26,622</u> | <u>21,464</u> |
| Operating transfers: | | |
| Operating transfers from the City and County of San Francisco | 19,037 | 19,037 |
| Operating transfers to the City and County of San Francisco | <u>(42,703)</u> | <u>(45,703)</u> |
| Net operating transfers | <u>(23,666)</u> | <u>(26,666)</u> |
| Net income (loss) | 2,956 | (5,202) |
| Retained earnings at beginning of year | <u>252,766</u> | <u>257,968</u> |
| Retained earnings at end of year | \$ <u>255,722</u> | <u>252,766</u> |

See accompanying notes to financial statements.

HETCH HETCHY WATER AND POWER

Statements of Cash Flows

Year ended June 30, 1999

(with comparative amounts for June 30, 1998)

(dollars in thousands)

| | 1999 | 1998 |
|---|-----------|----------|
| Cash flows from operating activities: | | |
| Cash received from customers, including cash deposits | \$ 44,332 | 36,908 |
| Cash received from quasi-external transactions | 41,241 | 41,234 |
| Cash received from tenants for rent | 150 | 127 |
| Cash paid to employees for services | (10,826) | (10,359) |
| Cash paid to suppliers for goods and services | (26,820) | (31,609) |
| Cash paid to other governments | (4,996) | (4,559) |
| Cash paid for fees, licenses and permits | (1,810) | (1,430) |
| Cash paid for judgements and claims | (175) | (260) |
| Cash paid for quasi-external transactions | (6,498) | (5,013) |
| Net cash provided by operating activities | 34,598 | 25,039 |
| Cash flows from noncapital financing activities: | | |
| Operating grants | 178 | 472 |
| Operating transfers in | 19,037 | 19,037 |
| Operating transfers out | (42,703) | (45,703) |
| Net cash used in noncapital financing activities | (23,488) | (26,194) |
| Cash flows from capital and related financing activities: | | |
| Acquisition and construction of capital assets | (6,820) | (4,797) |
| Payment of capital lease obligations | (55) | (51) |
| Net cash used in capital and related financing activities | (6,875) | (4,848) |
| Cash flows from investing activities: | | |
| Interest income received | 2,597 | 2,965 |
| Other investing activities | 175 | 145 |
| Net cash provided by investing activities | 2,772 | 3,110 |
| Increase (decrease) in cash and cash equivalents | 7,007 | (2,893) |
| Cash and cash equivalents: | | |
| Beginning of year | 49,828 | 52,721 |
| End of year | \$ 56,835 | 49,828 |

HETCH HETCHY WATER AND POWER

Statements of Cash Flows

Year ended June 30, 1999

(with comparative amounts for June 30, 1998)

(dollars in thousands)

| | 1999 | 1998 |
|---|------------------|---------------|
| Reconciliation of operating income to net cash provided by operating activities: | | |
| Operating income | \$ 24,030 | 18,088 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | |
| Depreciation and amortization | 8,383 | 8,131 |
| Changes in assets and liabilities: | | |
| Receivables: | | |
| Charges for services | (1,014) | (3,462) |
| Due from City and County of San Francisco | (3,001) | (1,606) |
| Other | 1,252 | (1,733) |
| Materials and supplies | (22) | (19) |
| Accounts payable | 2,441 | 5,264 |
| Accrued payroll | 80 | 84 |
| Accrued vacation, sick leave, and workers' compensation | 447 | 355 |
| Damage and claims liability | 2,085 | — |
| Deposits, advances and other liabilities | (83) | (63) |
| Net cash provided by operating activities | \$ <u>34,598</u> | <u>25,039</u> |
| Reconciliation of cash and cash equivalents to the balance sheet: | | |
| Deposits and investments with City Treasury | \$ 56,390 | 49,489 |
| Deposits and investments outside City Treasury | 14 | 339 |
| Total deposits and investments | 56,404 | 49,828 |
| Add unrealized loss on investments | 431 | — |
| Cash and cash equivalents at end of year on statements of cash flows | \$ <u>56,835</u> | <u>49,828</u> |

See accompanying notes to financial statements.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(1) The Financial Reporting Entity

Hetch Hetchy Water and Power (Hetch Hetchy) was established as a result of the Raker Act of 1913, which granted water and power resources rights-of-way on the Tuolumne River in Yosemite National Park to the City of San Francisco. Hetch Hetchy is engaged in the collection and distribution of approximately 85% of San Francisco's water supply and in the generation and transmission of electricity from that resource. Approximately one-third of the electricity is used by the San Francisco's municipal customers (e.g., the San Francisco Municipal Railway, the Recreation and Parks Department, the Port of San Francisco, San Francisco County hospitals, street lighting, Moscone Center, and the water and sewer utilities). The balance of the power generated is sold to other publicly owned utilities, such as the Modesto and Turlock Irrigation Districts. Hetch Hetchy consists of a system of reservoirs, hydroelectric power plants, aqueducts, pipelines, and transmission lines. This system carries water and power more than 165 miles from the Sierra Nevada to customers in the City of San Francisco and portions of the surrounding San Francisco Bay Area.

The San Francisco Public Utilities Commission (the Commission), established in 1932, is responsible for providing operational oversight of the public utility enterprises of the City and County of San Francisco (the City), which include Hetch Hetchy along with the City's water and sewer utilities (e.g., the San Francisco Water Department and the San Francisco Clean Water Program). The Commission consists of five members appointed by the Mayor who are responsible for determining such matters as the rates and charges for services, approval of contracts, and organizational policy. The Commission is a department of the City and, as such, the financial operations of Hetch Hetchy, the San Francisco Water Department, and the San Francisco Clean Water Program are included in the Comprehensive Annual Financial Report of the City as enterprise funds. These financial statements present only the financial operations of the Hetch Hetchy and are not intended to present the financial position of the City, the results of its operations and the cash flows of its proprietary fund types.

(2) Significant Accounting Policies

(a) *Basis of Accounting—Fund Accounting*

The accounts of Hetch Hetchy are organized on the basis of a proprietary fund type, specifically an enterprise fund. The operations of this fund are accounted for with a separate set of self-balancing accounts that comprise Hetch Hetchy's assets, liabilities, fund equity, revenues, and expenses. Enterprise Funds account for operations (i) that are financed and operated in a manner similar to private business enterprises where the intent of the Commission is that Hetch Hetchy's costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (ii) where the Commission has decided that periodic determination of revenues earned, expenses incurred, and net income or loss of Hetch Hetchy is appropriate for capital maintenance, public policy, management control, accountability, or other purpose.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(b) *Measurement Focus*

The financial activities of Hetch Hetchy are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Under this method, all assets and liabilities associated with operations are included on the balance sheet; revenues are recorded when earned, and expenses are recorded when liabilities are incurred.

Hetch Hetchy does not apply Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989. Hetch Hetchy applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as statements and interpretations of FASB, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

(c) *Cash and Cash Equivalents*

Cash and cash equivalents include all highly liquid investments, including restricted assets, with an original purchased maturity of three months or less.

(d) *Investments*

Certain investments are stated at fair value based on quoted market prices. Changes in fair value are recognized as investment income.

Money market funds that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost.

(e) *Inventory*

Inventory primarily consists of construction materials and maintenance supplies and is generally valued at cost or average cost. Inventory is expensed as it is consumed.

(f) *Property, Plant, and Equipment*

Property, plant, and equipment are stated at cost. Depreciation and amortization are computed by using the straight-line method based on the estimated useful lives of the related assets, which range from 3 to 75 years for equipment and 3 to 173 years for buildings, structures, and improvements. No depreciation or amortization is recorded in the year of acquisition, and a full year's depreciation or amortization is recorded in the year of disposal.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(g) Construction in Progress

The cost of acquisition and construction of major plant and equipment is recorded as construction in progress. As facilities are accepted by Hetch Hetchy and become operative, they are transferred to the plant and equipment accounts, and depreciated in accordance with Hetch Hetchy's depreciation policies. Costs of construction projects which are discontinued are recorded as expense in the year in which the decision is made to discontinue such projects.

(h) Accrued Vacation, Sick Leave, and Workers' Compensation

Accrued vacation pay, which may be accumulated up to ten weeks per employee, is charged to expense as earned. Unused sick leave accumulated through December 6, 1978 is vested and payable upon termination of employment by retirement, death, or disability caused by industrial accident. Sick leave earned subsequent to that date is nonvesting and may be accumulated up to six months per employee. Hetch Hetchy is self-insured for workers' compensation claims and accrues the estimated cost of those claims, including the estimated cost of incurred but not reported claims.

(i) Damage and Claims Liability

Hetch Hetchy is self-insured for general liability and property damage claims. The liability represents an estimate of the cost of all outstanding claims, including adverse loss development, and estimated incurred but not reported claims.

(j) Income Taxes

As a government agency, Hetch Hetchy is exempt from both federal income taxes and California state franchise taxes.

(k) Revenue Recognition

Revenues from water and power services furnished to consumers are recorded in the financial statements in the period that meters are read.

(l) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(m) Reclassifications

Certain reclassifications have been made to the 1998 financial statements to conform to the 1999 presentation. These reclassifications did not change total assets, liabilities, equity, or net income.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(3) Cash and Investments

The captions on the balance sheet related to cash and investments as of June 30 are as follows:

| | <u>1999</u> | <u>1998</u> |
|--|------------------|---------------|
| Deposits and investments with City Treasury | \$ 56,390 | 49,489 |
| Deposits and investments outside City Treasury | <u>14</u> | <u>339</u> |
| | <u>\$ 56,404</u> | <u>49,828</u> |

Investments

Hetch Hetchy's deposits and investments with the City Treasury are invested pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy guidelines are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The City's Comprehensive Annual Financial Report categorizes the level of custodial risk associated with its pooled cash and investments, which includes \$56,390 and \$49,489 of Hetch Hetchy's total deposits and investments as of June 30, 1999 and 1998, respectively. The City Treasurer allocates monthly income from the investment of pooled cash in proportion to Hetch Hetchy's end-of-month balances.

(4) Property, Plant, and Equipment

Property, plant, and equipment as of June 30 consisted of the following:

| | <u>1999</u> | <u>1998</u> |
|--|-------------------|------------------|
| Land | \$ 4,215 | 4,215 |
| Buildings, structures, and improvements | 375,390 | 370,207 |
| Equipment | 26,614 | 22,762 |
| Construction-in-progress | <u>9,964</u> | <u>10,574</u> |
| | 416,183 | 407,758 |
| Less accumulated depreciation and amortization | <u>(212,943)</u> | <u>(204,610)</u> |
| | <u>\$ 203,240</u> | <u>203,148</u> |

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(5) Employee Benefits

(a) *Retirement Plan*

Plan Description—The City has a single-employer defined benefit retirement plan (the Plan) which is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). The Plan covers substantially all full-time employees of Hetch Hetchy along with other employees of the City. The Plan provides basic service retirement, disability and death benefits based on specified percentages of final average salary, and provides cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City and County Employees' Retirement System, 1155 Market Street, 2nd Floor, San Francisco, CA 94103, or by calling (415) 554-1520.

Funding Policy—Contributions are made to the basic plan by both Hetch Hetchy and employees. Employee contributions are mandatory. Employee contribution rates for 1999 varied from 7% to 8% as a percentage of covered salary. Hetch Hetchy is required to contribute at an actuarially determined rate. No Hetch Hetchy contributions were required in 1999 as the actuarially determined contribution rate as a percentage of covered payroll was 0%. Hetch Hetchy's contributions to the Retirement System on behalf of its employees amounted to \$611, \$540, and \$545, for the years ended June 30, 1999, 1998, and 1997, respectively, which was equal to the required employee contributions for those years.

(b) *Health Care Benefits*

Health care benefits of Hetch Hetchy's employees, retired employees, and surviving spouses are financed by beneficiaries and the City through the City and County of San Francisco Health Service System, an internal service fund. Hetch Hetchy's contributions covering current and retired employees, which amounted to approximately \$880 and \$850 in fiscal years 1999 and 1998, respectively, are determined by Charter provisions based on similar contributions made by the ten most populous counties in California. Hetch Hetchy's liability for both current employee and postretirement health care benefits is limited to its annual contribution.

(6) Related Parties

Included in 1999 and 1998 operating revenues are sales of power to departments within the City of \$41,241 and \$41,234, respectively.

Income from Hetch Hetchy is available for certain operations of the City. During the years ended June 30, 1999 and 1998, Hetch Hetchy transferred \$42,703 and \$45,703, respectively, to the General Fund.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

A variety of City departments provide services such as engineering, purchasing, legal, data processing, telecommunication and human resources to Hetch Hetchy and charge amounts designed to recover those departments' costs. These charges totaling approximately \$1,200 and \$1,800 for the years ended June 30, 1999 and 1998, respectively, have been included in services provided by other departments in the accompanying financial statements.

Certain administrative costs of the Commission are allocated to Hetch Hetchy. For the years ended June 30, 1999 and 1998, the Commission allocated \$4,728 and \$2,818, respectively, in administrative costs to Hetch Hetchy which are included in general and administrative expenses in the accompanying financial statements.

The San Francisco Water Department buys water from Hetch Hetchy. This amount, totaling \$19,037 for both the years ended June 30, 1999 and 1998, has been included in operating transfers in the accompanying financial statements.

Hetch Hetchy serves as an intermediary agency between the Pacific Gas & Electric Company (PG&E) and all City departments for the design and construction of various electrical components and other related systems needed to deliver electricity. As an intermediary agency, Hetch Hetchy is responsible for the payment of all invoices to PG&E and its subcontractors. The total cost of the facilities including certain labor and administration costs incurred by Hetch Hetchy are charged back to the related departments. As of June 30, 1999, various City departments were indebted to Hetch Hetchy for unrecovered construction costs of approximately \$4.8 million, and this amount is included in the amount due from the City and County of San Francisco in the accompanying financial statements.

(7) Contributed Capital

The San Francisco International Airport (the Airport) is currently undergoing a major expansion project that will substantially increase future demand for electrical power. In December 1994, the City entered into two special facilities agreements (the Agreements) with PG&E to increase the capacity of existing PG&E equipment and systems at the Airport and Millbrae Substations to accommodate the Airport's projected increased load. Subsequent to seeking approval from the Federal Energy Regulatory Commission (FERC), staff from the Airport and Hetch Hetchy developed an alternate project configuration. Under the alternate configuration, PG&E would construct a new City-owned substation to be located on Airport property and would replace existing PG&E equipment at the current Airport Substation with City-owned equipment. Under the conditions of the alternate project configuration, PG&E would convey to the City, all rights, title and interests that PG&E has with regards to the new facilities upon their completion. In accordance with standard utility practice, the cost of these facilities was funded entirely by the Airport, and upon completion of each project phase, Hetch Hetchy would receive title to these assets from PG&E on behalf of the City. In addition, as the City's electric utility, Hetch Hetchy would assume responsibility for the operations, maintenance, repair and replacement of the facilities following their initial year of operation.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

During fiscal year 1999, PG&E conveyed title to one of the facilities and associated equipment to Hetch Hetchy pursuant to the alternate project configuration. The combined cost of the facilities and equipment that was contributed to Hetch Hetchy amounted to approximately \$1.7 million.

In July 1999, PG&E conveyed title to the remaining facilities and associated equipment to Hetch Hetchy pursuant to the alternate project configuration. The total cost of the remaining facilities and equipment that was contributed to Hetch Hetchy amounted to approximately \$5.3 million.

(8) Risk Management

Hetch Hetchy is self-insured for general liabilities, property damage, and workers' compensation claims. The risk of loss is managed internally by setting aside assets for claim settlement and recording a liability representing an estimate of the cost of all outstanding claims and incurred but not reported claims. Claim liabilities are recorded when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount and, therefore, it is reasonably possible that claim liabilities could change in the future. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and legal factors. The liabilities have been actuarially determined. Changes in the reported liability for the years ended June 30, 1999 and 1998 resulted from the following:

| | <u>1999</u> | <u>1998</u> |
|--|-----------------|--------------|
| Beginning-of-year liability | \$ 698 | 513 |
| Current year claims and changes in estimates | 2,565 | 445 |
| Current year claims payments | <u>(175)</u> | <u>(260)</u> |
| End of the year liability | <u>\$ 3,088</u> | <u>698</u> |
| General liabilities and property damage | \$ 2,330 | 245 |
| Workers' compensation | <u>758</u> | <u>453</u> |
| | <u>\$ 3,088</u> | <u>698</u> |

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(9) Commitments and Litigation

(a) *Commitments*

The Commission has contracted with PG&E to provide transmission capacity on PG&E's system where needed to deliver Hetch Hetchy's power to its customers. In addition, the PG&E agreement provides backup power and other support services to Hetch Hetchy. The PG&E agreement allows PG&E to review past billings paid by Hetch Hetchy and to retroactively adjust these payments to actual backup power, transmission and other charges as finally determined by PG&E. During fiscal years 1999 and 1998, Hetch Hetchy purchased \$13,365 and \$11,656, respectively, of transmission services, backup power and other support services from PG&E under the terms of the agreement.

To meet certain requirements of the Don Pedro Reservoir operating license, the City entered into an agreement with the Modesto and Turlock Irrigation Districts (the Districts) in which the Districts would be responsible for an increase in water flow releases from the reservoir in exchange for annual payments of \$3,500 from the City. The payments are to be made for the duration of the license, but may be terminated with one year's prior written notice after 2001. The City and the Districts have also agreed to monitor the fisheries in the lower Toulumne River for the duration of the license. A maximum monitoring expense of \$1,400 is to be shared between the City and the Districts over the term of the license. The City's share of the monitoring costs is 52% while the Districts are responsible for 48% of the costs.

As of June 30, 1999, Hetch Hetchy has outstanding commitments with third parties of \$3,453 for various capital projects and other purchase agreements for materials and services.

(b) *Litigation*

Hetch Hetchy is a defendant in various legal actions and claims that arise during the normal course of business, although the final disposition of these legal actions and claims is not determinable. However, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or results of operations of Hetch Hetchy.

**REQUIRED SUPPLEMENTARY INFORMATION –
YEAR 2000 READINESS INFORMATION**

HETCH HETCHY WATER AND POWER

Required Supplementary Information

Year 2000 Readiness Information

(unaudited)

(dollars in thousands)

The City is currently addressing Year 2000 issues relating to its computer systems and other electronic equipment. The Year 2000 issue refers to the fact that many computer programs use only the last two digits to refer to a year. Therefore, both 1900 and 2000 would be referred to as "00." Computer programs have to be adjusted to recognize the difference between those two years or the program may fail or create errors. Also, some programs may not be able to recognize that year 2000 is a leap year. Further, the Year 2000 issue could affect electronic equipment containing chips that have date recognition features. The Year 2000 issue may adversely affect the government's operations as early as the fiscal year 1999-2000.

(1) General Description

In 1995, the City began work on Year 2000 issues on a department-by-department basis. In 1998, the City established a central Year 2000 Program Management Office (PMO) expressly for the purpose of providing unified resources and oversight for the City departments' Year 2000 efforts. The PMO has focused City readiness efforts on "mission-critical systems," defined as those services or functions which, if disrupted, would have a direct and immediate impact on a citizen's health, safety or transportation. There are 14 City departments that provide mission critical services to the public.

The mission-critical departments were also instructed to use standardized forms and procedures to report to the PMO. The PMO staff collects the information submitted by departments and reports in turn to the City's Committee on Information Technology Year 2000 Subcommittee, the Board of Supervisors and the Mayor. The PMO also communicates the City's Year 2000 information to the public via the internet, community meetings, and other outreach efforts.

The PMO has assisted departments in conducting inventories and successive steps toward Year 2000 readiness. The PMO's standards have required mission-critical departments to identify those inventory items on which mission-critical systems depend. The PMO has also collected information about systems involving interdepartmental dependencies, where the responsibility for a particular system is not clear. For example, the Police, Fire and Sheriff departments all depend on telecommunications equipment, which is primarily the responsibility of the Department of Telecommunications and Information Services. The PMO has also facilitated the communications between the using departments and the supporting departments to make sure that remediation of particular systems is not delayed while the responsible department is identified, that the responsible department's work is not delayed by repetitive inquiries by multiple user departments, and that a remediation success is translated back to the readiness accounting for each department that uses that system.

Currently, the embedded system program is in the process of independent verification and validation by third party engineers, who are reviewing each step in the mission-critical departments' embedded systems review process and the adequacy of the associated documentation.

In addition, the PMO is currently assisting departments in the ongoing development and refinement of contingency plans. The PMO has provided detailed guidelines and procedures for developing contingency plans, and a uniform format so that the plans can be independently reviewed as part of the PMO's independent verification and validation program.

HETCH HETCHY WATER AND POWER

Required Supplementary Information

Year 2000 Readiness Information

(unaudited)

(dollars in thousands)

(2) Stages of Work

The City has identified 14 departments that provide mission critical services to the public. Each of these departments is responsible for performing the following stages of work with respect to the systems and equipment necessary to provide the mission-critical services:

- Awareness stage – Establishing a budget and project plan for dealing with the Year 2000 issue
- Assessment stage – Identifying the systems and components for which Year 2000 compliance work is needed
- Remediation stage – Making changes to systems and equipment
- Validation/testing stage – Validating and testing the changes that were made during the remediation stage

The Commission has completed the awareness and assessment stages for the following mission-critical systems and electronic equipment:

- Water distribution
- Water treatment
- Wastewater collection
- Wastewater treatment
- Power generation
- Power distribution

The remediation and validation/testing stages of the Commission, along with a high level independent verification and validation by third party engineers through the PMO's office, are scheduled to be completed by November 15, 1999.

(3) Resources Committed

As of year-end, the Commission had outstanding commitments for addressing Year 2000 issues relating to its computer systems and other electronic equipment in the amount of \$235.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. While the City believes that mission-critical systems will function, management cannot assure that the City is or will be Year 2000 ready, that the City's remediation efforts will be successful in whole or in part or that parties with whom the City does business will be Year 2000 ready.

The City's Comprehensive Annual Financial Report provides additional information on how the City is addressing Year 2000 issues.



SAN FRANCISCO WATER DEPARTMENT

Financial Statements

June 30, 1999 and 1998

(With Independent Auditors' Report Thereon)

SAN FRANCISCO WATER DEPARTMENT

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Three Embarcadero Center
San Francisco, CA 94111

Independent Auditors' Report

Honorable Mayor and Board of Supervisors
City and County of San Francisco, California:

We have audited the accompanying financial statements of the San Francisco Water Department (the Department) of the City and County of San Francisco, California (the City), as of and for the year ended June 30, 1999, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 1, the financial statements present only the Department and are not intended to present fairly the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Francisco Water Department of the City and County of San Francisco, California, as of June 30, 1999, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

The Year 2000 supplementary information on pages 21 and 22 is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board, and we did not audit and do not express an opinion on such information. Further, we were unable to apply to the information certain procedures prescribed by professional standards because of the nature of the subject matter underlying the disclosure requirements and because sufficiently specific criteria regarding the matters to be disclosed have not been established. In addition, we do not provide assurance that the Department is or will become Year 2000 compliant, that the Department's Year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Department does business are or will become Year 2000 compliant.

KPMG LLP

October 22, 1999



KPMG LLP, KPMG LLP, a U.S. limited liability partnership, is
a member of KPMG International, a Swiss association

SAN FRANCISCO WATER DEPARTMENT

Balance Sheets

June 30, 1999

(With comparative amounts for June 30, 1998)

(dollars in thousands)

| Assets | 1999 | 1998 |
|---|------------|---------|
| Current assets: | | |
| Deposits and investments with City Treasury | 64,750 | 75,864 |
| Deposits and investments outside City Treasury | 67 | 51 |
| Receivables: | | |
| Charges for services (net of allowance for doubtful accounts of \$980 in 1999 and 1998) | 8,834 | 9,325 |
| Suburban water rate agreement | 5,807 | — |
| Interest and other | 1,728 | 1,262 |
| Total receivables | 16,369 | 10,587 |
| Materials and supplies – at average cost | 802 | 782 |
| Total current assets | 81,988 | 87,284 |
| Restricted assets: | | |
| Deposits and investments with City Treasury | 56,858 | 74,348 |
| Deposits and investments outside City Treasury | 9,655 | 9,151 |
| Interest receivable | 1,291 | 545 |
| Total restricted assets | 67,804 | 84,044 |
| Property, plant and equipment, net of accumulated depreciation | 429,755 | 409,295 |
| Bond issuance costs, net of accumulated amortization of \$1,086 in 1999 and \$972 in 1998 | 1,925 | 2,033 |
| Total assets | \$ 581,472 | 582,656 |
| Liabilities and Equity | | |
| Current liabilities: | | |
| General obligation bonds, current portion | \$ 830 | 1,340 |
| Revenue bonds, current portion | 6,585 | 5,100 |
| Accounts payable | 3,920 | 3,564 |
| Accrued payroll | 3,634 | 2,938 |
| Accrued vacation, sick leave, and workers' compensation, current portion | 3,673 | 3,544 |
| Bond interest payable | 2,288 | 2,349 |
| Suburban water rate agreement | — | 7,370 |
| Damage and claims liability, current portion | 739 | 3,260 |
| Deposits, advances and other liabilities | 2,441 | 2,339 |
| Total current liabilities | 24,110 | 31,804 |
| Liabilities payable from restricted assets | 1,489 | 767 |
| Long-term liabilities: | | |
| Accrued vacation, sick leave, and workers' compensation | 5,466 | 4,355 |
| Damage and claims liability | 2,705 | 2,580 |
| Total long-term liabilities | 8,171 | 6,935 |
| Long-term debt, less current portion: | | |
| General obligation bonds | — | 830 |
| Revenue bonds | 228,683 | 234,761 |
| Total long-term debt | 228,683 | 235,591 |
| Total liabilities | 262,453 | 275,097 |
| Equity: | | |
| Contributed capital | 75 | 75 |
| Retained earnings – reserved for bond requirements and other commitments | 7,169 | 6,580 |
| Retained earnings – unreserved | 311,775 | 300,904 |
| Total equity | 319,019 | 307,559 |
| Total liabilities and equity | \$ 581,472 | 582,656 |

See accompanying notes to financial statements.

SAN FRANCISCO WATER DEPARTMENT

Statements of Revenues, Expenses, and Changes in Retained Earnings

Year ended June 30, 1999

(With comparative amounts for the year ended June 30, 1998)

(dollars in thousands)

| | 1999 | 1998 |
|---|------------|----------|
| Operating revenues: | | |
| Charges for services | \$ 128,347 | 121,137 |
| Rental income | 7,201 | 6,254 |
| Other revenue | 3,060 | 2,070 |
| Total operating revenues | 138,608 | 129,461 |
| Operating expenses: | | |
| Personal services | 42,836 | 42,888 |
| Contractual services | 6,991 | 5,086 |
| Materials and supplies | 7,019 | 5,933 |
| Depreciation and amortization | 20,407 | 20,437 |
| General and administrative | 16,530 | 14,727 |
| Services provided by other departments | 7,900 | 4,815 |
| Bad debt expense | 190 | 47 |
| Other | 5,315 | 8,579 |
| Total operating expenses | 107,188 | 102,512 |
| Operating income | 31,420 | 26,949 |
| Nonoperating revenues (expenses): | | |
| Operating grant – federal | 615 | 554 |
| Operating grant – state | 110 | — |
| Interest and investment income | 6,929 | 10,116 |
| Interest expense | (13,435) | (15,832) |
| Gain on sale of property and equipment | 3,548 | 2,602 |
| Other, net | 1,600 | 2,409 |
| Net nonoperating expenses | (633) | (151) |
| Income before operating transfers | 30,787 | 26,798 |
| Operating transfers: | | |
| Operating transfers from the City and County of San Francisco | 1,406 | 1,410 |
| Operating transfers to the City and County of San Francisco | (20,733) | (20,447) |
| Net operating transfers | (19,327) | (19,037) |
| Net income | 11,460 | 7,761 |
| Retained earnings at beginning of year | 307,484 | 299,723 |
| Retained earnings at end of year | \$ 318,944 | 307,484 |

See accompanying notes to financial statements.

SAN FRANCISCO WATER DEPARTMENT

Statements of Cash Flows

Year ended June 30, 1999

(With comparative amounts for the year ended June 30, 1998)

(dollars in thousands)

| | 1999 | 1998 |
|---|------------|-----------|
| Cash flows from operating activities: | | |
| Cash received from customers, including cash deposits | \$ 118,087 | 122,279 |
| Cash received from tenants for rent | 7,502 | 6,254 |
| Cash paid to employees for services | (41,605) | (42,186) |
| Cash paid to suppliers for goods and services | (17,638) | (20,689) |
| Cash paid for judgements and claims | (3,830) | (1,355) |
| Cash paid for quasi-external transactions | (23,642) | (14,564) |
| Net cash provided by operating activities | 38,874 | 49,739 |
| Cash flows from noncapital financing activities: | | |
| Operating grants | 544 | 554 |
| Operating transfers in | 1,406 | 1,410 |
| Operating transfers out | (20,733) | (20,447) |
| Net cash used in noncapital financing activities | (18,783) | (18,483) |
| Cash flows from capital and related financing activities: | | |
| Proceeds from sale of fixed assets | 3,548 | 2,602 |
| Interest on long-term debt | (13,903) | (17,168) |
| Principal paid on long-term debt | (6,440) | (103,235) |
| Acquisition and construction of capital assets | (39,503) | (25,899) |
| Net cash used in capital and related financing activities | (56,298) | (143,700) |
| Cash flows from investing activities: | | |
| Interest income received | 6,350 | 8,152 |
| Proceeds from sale of investments | 85,399 | 376,229 |
| Purchase of investments | (110,265) | (285,584) |
| Other investing activities | 1,890 | 2,876 |
| Net cash (used in) provided by investing activities | (16,626) | 101,673 |
| Decrease in cash and cash equivalents | (52,833) | (10,771) |
| Cash and cash equivalents: | | |
| Beginning of year | 134,588 | 145,359 |
| End of year | \$ 81,755 | 134,588 |

See accompanying notes to financial statements.

SAN FRANCISCO WATER DEPARTMENT

Statements of Cash Flows

Year ended June 30, 1999

(With comparative amounts for the year ended June 30, 1998)

(dollars in thousands)

| | 1999 | 1998 |
|---|-----------|----------|
| Reconciliation of operating income to net cash provided by operating activities: | | |
| Operating income | \$ 31,420 | 26,949 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | |
| Depreciation and amortization | 20,407 | 20,437 |
| Provision for uncollectible accounts | 190 | 47 |
| Changes in assets and liabilities: | | |
| Receivables: | | |
| Charges for services, net | 301 | 1,875 |
| Suburban water rate agreement receivable | (5,807) | — |
| Other | (335) | 174 |
| Materials and supplies | (20) | 754 |
| Accounts payable | 356 | (1,452) |
| Accrued payroll | 696 | 552 |
| Accrued vacation, sick leave, and workers' compensation | 1,240 | 339 |
| Suburban water rate agreement liability | (7,370) | (2,352) |
| Due to City and County of San Francisco | — | (393) |
| Damage and claims liability | (2,396) | 3,260 |
| Deposits, advances and other liabilities | 192 | (451) |
| Net cash provided by operating activities | \$ 38,874 | 49,739 |
| Reconciliation of cash and cash equivalents to the balance sheet: | | |
| Deposits and investments with City Treasury: | | |
| Unrestricted | \$ 64,750 | 75,864 |
| Restricted | 56,858 | 74,348 |
| Deposits and investments outside City Treasury: | | |
| Unrestricted | 67 | 51 |
| Restricted | 9,655 | 9,151 |
| Total deposits and investments | 131,330 | 159,414 |
| Less deposits and investments not meeting the definition of cash equivalents | (49,575) | (24,826) |
| Cash and cash equivalents at end of year on statements of cash flows | \$ 81,755 | 134,588 |

See accompanying notes to financial statements.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(1) The Financial Reporting Entity

The San Francisco Water Department (the Department) was established in 1930 under the provisions of the City Charter of San Francisco. The Department acquired the fully developed, mature water works for San Francisco on March 3, 1930. Since then, the City and County of San Francisco (the City) has operated and maintained the water works as the San Francisco Water Department. The Board of Supervisors of the City has adopted resolutions (the Water Resolutions) providing for the issuance of various water revenue and refunding bond series. The Department, which consists of a system of reservoirs, storage tanks, water treatment plants, pump stations, and pipelines, is engaged in the distribution of water to San Francisco and certain suburban areas. On average, the Department delivers approximately 80,000,000 gallons of water per day to nearly 770,000 people within San Francisco and certain suburban areas.

The San Francisco Public Utilities Commission (the Commission), established in 1932, is responsible for providing operational oversight of the public utility enterprises of the City, which include the Department along with the City's power and sewer utilities (e.g., Hetch Hetchy Water and Power [Hetch Hetchy] and the San Francisco Clean Water Program). The Commission consists of five members appointed by the Mayor, who are responsible for determining such matters as the rates and charges for services, approval of contracts, and organizational policy. The Commission is a department of the City and, as such, the financial operations of the Department, Hetch Hetchy, and the San Francisco Clean Water Program are included in the Comprehensive Annual Financial Report of the City as enterprise funds. These financial statements present only the financial operations of the Department and are not intended to present the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types.

(2) Significant Accounting Policies

(a) *Basis of Accounting—Fund Accounting*

The accounts of the Department are organized on the basis of a proprietary fund type, specifically an enterprise fund. The operations of this fund are accounted for with a separate set of self-balancing accounts that comprise the Department's assets, liabilities, fund equity, revenues, and expenses. Enterprise Funds account for operations (i) that are financed and operated in a manner similar to private business enterprises where the intent of the Commission is that the Department's costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (ii) where the Commission has decided that periodic determination of revenues earned, expenses incurred, and net income or loss of the Department is appropriate for capital maintenance, public policy, management control, accountability, or other purpose.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(b) *Measurement Focus*

The financial activities of the Department are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Under this method, all assets and liabilities associated with its operations are included on the balance sheet; revenues are recorded when earned, and expenses are recorded when liabilities are incurred.

The Department does not apply Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989. The Department applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as statements and interpretations of the FASB, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

(c) *Cash and Cash Equivalents*

Cash and cash equivalents include all highly liquid investments, including restricted assets, with an original purchased maturity of three months or less.

(d) *Investments*

Certain investments are stated at fair value based on quoted market prices. Changes in fair value are recognized as investment income.

Money market funds and banker's acceptances that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost.

(e) *Inventory*

Inventory primarily consists of construction materials and maintenance supplies, and is generally valued at cost or average cost. Inventory is expensed as it is consumed.

(f) *Property, Plant, and Equipment*

Property, plant, and equipment are stated at cost. Depreciation is computed using the straight-line method based on the estimated useful lives of the related assets, which range from 3 to 75 years for equipment and 3 to 173 years for buildings, structures, and improvements. No depreciation is recorded in the year of acquisition, and a full year's depreciation is recorded in the year of disposal.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(g) *Construction in Progress*

The cost of acquisition and construction of major plant and equipment is recorded as construction in progress. As facilities are accepted by the Department and become operative, they are transferred to the plant and equipment accounts and depreciated in accordance with the Department's depreciation policies. Costs of construction projects which are discontinued are recorded as expense in the year in which the decision is made to discontinue the project.

(h) *Capitalization of Interest*

A portion of the interest cost incurred on capital projects is capitalized on assets which require a period of time for construction or to otherwise prepare them for their intended use. Such amounts are amortized over the useful lives of the assets.

(i) *Bond Discount and Issuance Costs*

Bond discount and issuance costs are amortized over the term of the related bonds.

(j) *Accrued Vacation, Sick Leave, and Workers' Compensation*

Accrued vacation pay, which may be accumulated up to ten weeks per employee, is charged to expense as earned. Unused sick leave accumulated through December 6, 1978 is vested and payable upon termination of employment by retirement, death, or disability caused by industrial accident. Sick leave earned subsequent to that date is nonvesting and may be accumulated up to six months per employee. The Department is self-insured for workers' compensation claims and accrues the estimated cost of those claims, including the estimated cost of incurred but not reported claims.

(k) *Damage and Claims Liability*

The Department is self-insured for general liability and property damage claims. The liability represents an estimate of the cost of all outstanding claims, including adverse loss development, and estimated incurred but not reported claims.

(l) *Arbitrage Rebate Payable*

Certain bonds are subject to arbitrage rebate requirements in accordance with regulations issued by the U.S. Treasury Department. The requirements generally stipulate that earnings from the investment of the tax-exempt bond proceeds that exceed related interest costs on the bonds must be remitted to the federal government on every fifth anniversary of each bond issue. The arbitrage rebate liability was approximately \$441 as of June 30, 1999 and 1998.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(m) *Refunding of Debt*

Gains or losses occurring from advance refundings of debt are deferred and amortized into interest expense over the remaining life of the old bonds or the life of the new bonds, whichever is shorter.

(n) *Income Taxes*

As a government agency, the Department is exempt from both federal income taxes and California state franchise taxes.

(o) *Revenue Recognition*

Revenues from water services furnished to consumers are recorded in the financial statements in the period that meters are read. In general, customers are billed on a cyclical basis with large commercial and industrial customers billed monthly, and all other customers bimonthly.

In June 1998, the voters passed Proposition H, which effectively froze the water rates at the levels in effect as of January 1, 1998 until July 1, 2006, subject to certain limitations such as to service pre-existing debt. The passage of Proposition H limits the Department's ability to fund future water system maintenance projects and/or meet new federal and state regulations that may arise during the period in which Proposition H is effective.

(p) *Use of Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(q) *Reclassifications*

Certain reclassifications have been made to the 1998 financial statements to conform to the 1999 presentation. These reclassifications did not change total assets, liabilities, equity, or net income.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(3) Cash and Investments

The captions on the balance sheet related to cash and investments as of June 30 are as follows:

| | 1999 | 1998 |
|---|-------------------|----------------|
| Deposits and investments with City Treasury: | | |
| Unrestricted – pooled | \$ 64,750 | 75,864 |
| Restricted – pooled and nonpooled (note 5) | 56,858 | 74,348 |
| Deposits and investments outside City Treasury: | | |
| Unrestricted | 67 | 51 |
| Restricted (note 5) | 9,655 | 9,151 |
| | <u>\$ 131,330</u> | <u>159,414</u> |

Investments

The Department's deposits and investments with the City Treasury are invested pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy guidelines are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The City's Comprehensive Annual Financial Report categorizes the level of custodial risk associated with the its pooled cash and investments, which includes \$69,202 and \$66,306 of the Department's total deposits and investments with the City Treasury as of June 30, 1999 and 1998, respectively. The City Treasurer allocates monthly income from the investment of pooled cash in proportion to the Department's end-of-month balances.

The Department is required by its bond indentures to maintain certain revenue bond funds in government obligations, time deposits, or demand deposits. The Department follows the investment policy guidelines of the City Treasurer for its other investments, including those investments held by trustees.

The Department's investments, including those held by trustees, are categorized below to give an indication of the level of custodial risk assumed at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the Department or its agent in the name of the Department. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the name of the Department. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the name of the Department.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

The Department's investment portfolio is stated at fair value (except for money market funds and banker's acceptances, which are stated at amortized cost, which approximates market). Fair value is based on quotes obtained from national exchanges as of June 30, 1999.

| | Category | | | Carrying value |
|---|------------------|----------|----------|-------------------|
| | 1 | 2 | 3 | |
| Banker's acceptances | \$ 10,907 | — | — | 10,907 |
| U.S. Treasury bills | 9,682 | — | — | 9,682 |
| Commercial paper | 1,994 | — | — | 1,994 |
| Other U.S. government securities | 39,479 | — | — | 39,479 |
| | <u>\$ 62,062</u> | <u>—</u> | <u>—</u> | <u>62,062</u> |
| Money market funds | | | | 26 |
| Imprest Fund | | | | 40 |
| Pooled cash and investments held by the City Treasurer | | | | 69,202 |
| | | | | <u>\$ 131,330</u> |

(4) Property, Plant, and Equipment

Property, plant, and equipment as of June 30 consisted of the following:

| | 1999 | 1998 |
|--|-------------------|------------------|
| Land | \$ 17,217 | 17,220 |
| Buildings, structures, and improvements | 601,426 | 580,314 |
| Equipment | 52,672 | 44,968 |
| Construction-in-progress | 40,670 | 28,828 |
| | <u>711,985</u> | <u>671,330</u> |
| Less accumulated depreciation and amortization | <u>(282,230)</u> | <u>(262,035)</u> |
| | <u>\$ 429,755</u> | <u>409,295</u> |

During the years ended June 30, 1999 and 1998, the Department incurred total interest cost of \$14,173 and \$16,378, respectively. Of the total amount of interest cost incurred, \$738 and \$546 was capitalized into the cost of constructed assets during the years ended June 30, 1999 and 1998, respectively.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(5) Restricted Assets

Pursuant to the Water Resolutions, all revenues of the Department (except amounts on deposit in the rebate fund) are irrevocably pledged to the punctual payment of debt service on the Water Revenue and Refunding Bonds. Accordingly, the revenues of the Department shall not be used for any other purpose while any of its Water Revenue and Refunding Bonds are outstanding, except as expressly permitted by the Water Resolutions. Further, all revenues shall be deposited by the City Treasurer in special funds designated as the Water Department Revenue Fund (the Water Revenue Fund), which must be maintained in the City Treasury. Deposits in the Water Revenue Fund, including earnings thereon, shall be appropriated, transferred, expended, or used for the following purposes pertaining to the financing, maintenance, and operation of the Department in accordance with the following priority:

1. The payment of operation and maintenance expenses for such utility and related facilities.
2. The payment of pension charges and proportionate payments to such compensation and other insurance or outside reserve funds as the Department may establish or the Board of Supervisors may require with respect to employees of the Department.
3. The payment of principal, interest, reserve, sinking fund, and other mandatory funds created to secure Revenue Bonds issued by the Department for the acquisition, construction, or extension of facilities owned, operated, or controlled by the Department.
4. The payment of principal and interest on General Obligation Bonds issued by the City for the Department's purposes.
5. Reconstruction and replacement as determined by the Department or as required by any of the Department's Revenue Bond ordinance duly adopted and approved.
6. The acquisition of land, real property, or interest in real property for, and the acquisition, construction, enlargement, and improvement of, new and existing buildings, structures, facilities, equipment, appliances, and other property necessary or convenient to the development or improvement of such utility owned, controlled, or operated by the Department; and for any other lawful purpose of the Department including the transfer of surplus funds pursuant to Section 6.407(e) of the City's Charter.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

In accordance with the Water Resolutions, the Department maintains certain restricted cash and investment balances in trust. Restricted assets held in trust consisted of the following as of June 30:

| | <u>1999</u> | <u>1998</u> |
|---|-------------------------|----------------------|
| Equity in deposits and investments of the City Treasurer: | | |
| Water Bond Construction Fund | \$ <u>56,858</u> | <u>74,348</u> |
| Total | <u>56,858</u> | <u>74,348</u> |
| Investments held by trustee: | | |
| 1991 Water Revenue Bond Fund | 3,615 | 3,700 |
| 1992 Water Revenue Bond Fund | 3,486 | 3,459 |
| 1996 Water Revenue Bond Fund | <u>2,554</u> | <u>1,992</u> |
| Total | <u>9,655</u> | <u>9,151</u> |
| Interest receivable: | | |
| Water Bond Construction Fund | <u>1,291</u> | <u>545</u> |
| Total | <u>1,291</u> | <u>545</u> |
| Total restricted assets | \$ <u><u>67,804</u></u> | <u><u>84,044</u></u> |

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(6) Long-Term Debt

Long-term debt consisted of the following as of June 30:

| | Interest rates | Due serially to | 1999 | 1998 |
|---|-------------------|--------------------|-------------------|-----------------|
| General obligation bonds: | | | | |
| 1972 Municipal Water System Bonds | 4%-5.7% | 2000 | \$ 830 | 2,170 |
| Less current portion of general obligation bonds | | | <u>830</u> | <u>1,340</u> |
| Long-term portion of general obligation bonds | | | <u>\$ —</u> | <u>830</u> |
| Revenue Bonds: | | | | |
| 1991 Water Revenue Bonds | 5.3%-7.4% | 2021 | \$ 10,354 | 11,659 |
| 1992 Water Revenue Refunding Bonds | 5.35%-6.5% | 2016 | 103,705 | 107,180 |
| 1996 Water Revenue Refunding Bonds | 5%-6.5% | 2026 | 131,255 | 131,455 |
| Unamortized bond discount and refunding loss | | | <u>(10,046)</u> | <u>(10,433)</u> |
| Total revenue bonds | | | 235,268 | 239,861 |
| Less current portion of revenue bonds | | | <u>(6,585)</u> | <u>(5,100)</u> |
| Long-term portion of revenue bonds | | | <u>\$ 228,683</u> | <u>234,761</u> |

The payments of principal and interest amounts on various bonds are collateralized by future water revenues.

(a) General Obligation Bonds

During 1972, the Department issued \$39,000 of General Obligation Bonds relating to the municipal water system. The bonds have interest rates ranging from 4% to 5.7% and will be paid in full in fiscal year 2000.

The Department has complied with the debt covenants of the General Obligation Bonds.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(b) Water Revenue Bonds Series 1991

During fiscal year 1991, the Department issued Revenue Bonds of approximately \$70,146 with interest varying from 5% to 7.4%. The Revenue Bonds include current interest serial and term bonds with an original principal amount of approximately \$92,985, and serial capital appreciation bonds with an original principal amount of approximately \$1,051. The current interest serial bonds mature through November 1, 2007, and the current interest term bonds mature on November 1, 2010, 2017 and 2020. The serial capital appreciation bonds mature from November 1, 2018 through November 1, 2019. Interest on the capital appreciation bonds is due upon maturity, and is recognized as annual interest expense over the life of the bonds using the interest method. The Department has recognized approximately \$769 and \$647 of unpaid interest on the capital appreciation bonds as of June 30, 1999 and 1998, respectively, and has included it with the outstanding principal balance of the bonds.

(c) Water Revenue Refunding Bonds Series 1992

In fiscal 1992, the Department issued \$107,180 of Revenue Refunding Bonds (the 1992 Refunding Bonds) pursuant to a crossover refunding of 1987 Water Revenue Refunding Bonds. The proceeds were used to purchase U.S. government securities which were placed into an irrevocable trust to be used for the payment of interest on the 1992 Refunding Bonds, and \$460 per year of principal due on the 1987 Refunding Bonds through November 1, 1997 (crossover date), at which time the remaining proceeds were used to advance refund the 1987 Refunding Bonds which amounted to \$102,570 including a call premium of \$860 and additional interest of \$1,114. The debt service requirements of the 1992 Refunding Bonds after the crossover date are being made from the net revenues of the Department.

(d) Water Revenue Refunding Bonds Series 1996

In fiscal 1997, the Department issued \$131,470 (face value) of 1996 Series A Water Revenue Bonds. A portion of the bond proceeds was designated for the purpose of refunding \$53,090 (face value) of 1991 Revenue Bonds which were due serially to 2020. The funding extended maturities on the bonds in order to lower required annual payments. After payment of \$852 in issue costs, \$57,012 of the net bond proceeds was transferred to a trustee to be placed in an irrevocable trust to redeem the refunded portion of the 1991 Revenue Bonds. Accordingly, the refunded portion of the 1991 Revenue Bonds was removed from the Department's balance sheet. The advance refunding decreased the Department's total debt service payment over the next 29 years by \$2,475, and provided for an economic gain of \$4,064. The resulting accounting loss of \$5,989 has been deferred and is being amortized over the remaining life of the old debt. As of June 30, 1999 and 1998, the unamortized portion of the accounting loss was \$5,144 and \$5,471 respectively.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(e) *Future Annual Debt Service of Revenue Bonds*

The future annual debt service relating to the Revenue Bonds outstanding as of June 30, 1999 is as follows:

| | <u>Principal</u> | <u>Interest</u> |
|--|--------------------------|--------------------------|
| Year ending June 30: | | |
| 2000 | \$ 6,585 | 13,488 |
| 2001 | 6,955 | 13,108 |
| 2002 | 7,350 | 12,699 |
| 2003 | 7,775 | 12,247 |
| 2004 | 8,260 | 11,748 |
| Thereafter | <u>208,389</u> | <u>105,765</u> |
| | 245,314 | \$ <u><u>169,055</u></u> |
| Less: | | |
| Current portion | (6,585) | |
| Unamortized bond discount and refunding loss | <u>(10,046)</u> | |
| Long-term portion as of June 30, 1999 | \$ <u><u>228,683</u></u> | |

As defined in the Water Resolutions, the principal and interest of the Department's Revenue and Refunding Bonds are payable from its corresponding revenue as well as monies deposited in certain funds and accounts pledged thereto (note 5).

The Department has complied with the debt covenants of the Revenue Bonds.

(f) *Authorized and Unissued Debt*

In November 1997, the voters approved the issuance of \$304,000 in water revenue bonds. In May 1999, the City's Board of Supervisors authorized the Commission to issue up to \$140,000 of the water revenue bonds that were previously approved by the voters. As of June 30, 1999, the \$140,000 of water revenue bonds remained unissued.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(7) Suburban Water Rate Agreement

During 1984, the City entered into a Settlement Agreement and Master Water Sales Contract (the Suburban Water Rate Agreement) with certain suburban customers, which establishes water rates to be charged to those customers (the Suburban Purchasers). Pursuant to the terms of the Suburban Water Rate Agreement, the City is required to establish water rates applicable to the Suburban Purchasers at the beginning of each fiscal year. The suburban water rates are based on an estimate of the level of revenues necessary to recoup the cost of distributing water to the Suburban Purchasers based on the methodology outlined in Article IV of the Suburban Water Rate Agreement (the Suburban Revenue Requirement). During fiscal years 1999 and 1998, the Suburban Revenue Requirement charged to such suburban customers was \$64,537 and \$63,917, respectively. Such amounts are subject to final review by the suburban customers, based on the Suburban Revenue Requirement calculation.

Pursuant to Article V, Section 5.07 of the Suburban Water Rate Agreement, the City is required to recompute the Suburban Revenue Requirement after the close of each fiscal year based on the actual costs incurred in the delivery of water to the Suburban Purchasers. The difference between the suburban revenues earned during the year and the "actual" Suburban Revenue Requirement is recorded in a separate account (the Balancing Account) and represents the cumulative amount that is either owed to the Suburban Purchasers (if the suburban revenues exceed the Suburban Revenue Requirement) or owed to the City (if the Suburban Revenue Requirement exceeds the suburban revenues paid). In accordance with Article V of the Suburban Water Rate Agreement, the amount recorded in the Balancing Account shall earn interest at a rate equal to the average rate received by the City during the year on the invested pooled funds of the City Treasurer, and shall be taken into consideration in the determination of subsequent suburban water rates. Upon the expiration of the Suburban Water Rate Agreement, the remaining balance in the Balancing Account shall be settled between the City and the Suburban Purchasers. As of June 30, 1999, the Suburban Purchasers owed the Department approximately \$5,800 under the terms of the Suburban Water Rate Agreement. As of June 30, 1998, the Department owed the Suburban Purchasers approximately \$7,400 under the terms of the Suburban Water Rate Agreement.

(8) Employee Benefits

(a) Retirement Plan

Plan Description—The City has a single-employer defined benefit retirement plan (the Plan) which is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). The Plan covers substantially all full-time employees of the Department along with other employees of the City. The Plan provides basic service retirement, disability, and death benefits based on specified percentages of final average salary, and provides cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City and

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

County Employees' Retirement System, 1155 Market Street, 2nd Floor, San Francisco, CA 94103, or by calling (415) 554-1520.

Funding Policy—Contributions are made to the basic plan by both the Department and its employees. Employee contributions are mandatory. Employee contribution rates for 1999 and 1998 varied from 7% to 8% as a percentage of covered salary. The Department is required to contribute at an actuarially determined rate. No Department contributions were required for 1999 and 1998 as the actuarially determined contribution rate as a percentage of covered payroll was 0%. The Department's contributions to the Retirement System on behalf of its employees amounted to \$1,715, \$1,579 and \$1,503 for the years ended June 30, 1999, 1998, and 1997, respectively, which was equal to the required employee contributions for those years.

(b) Health Care Benefits

Health care benefits of the Department's employees, retired employees, and surviving spouses are financed by beneficiaries and the City through the City and County of San Francisco Health Service System, an internal service fund. The Department's contributions covering current and retired employees, which amounted to approximately \$2,318 and \$2,038 in fiscal years 1999 and 1998, respectively, is determined by Charter provisions based on similar contributions made by the ten most populous counties in California. The Department's liability for both current employee and postretirement health care benefits is limited to its annual contribution.

(9) Related Parties

During 1999 and 1998, the Department delivered water without charge to certain City departments which amounted to approximately \$4,700 and \$5,300, respectively, based on metered usage and applicable water rates, which has been excluded from operating revenues in the accompanying financial statements.

Certain administrative costs of the Commission are allocated to the Department. For the years ended June 30, 1999 and 1998, the Commission allocated \$14,927 and \$9,778, respectively, in administrative costs to the Department, which are included in general and administrative expenses in the accompanying financial statements.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

The Department buys water from Hetch Hetchy. This amount, totaling \$19,037 for the years ended June 30, 1999 and 1998, respectively, has been included in operating transfers in the accompanying financial statements.

The Department purchases electricity from Hetch Hetchy at market rates. This amount, totaling \$3,822 and \$3,809 for the years ended June 30, 1999 and 1998, respectively, has been included in services provided by other departments in the accompanying financial statements.

A variety of City departments provide services such as engineering, purchasing, legal, data processing, telecommunication and human resources to the Department and charge amounts designed to recover those departments' costs. These charges totaling approximately \$3,800 and \$1,000 for the years ended June 30, 1999 and 1998, respectively, have been included in services provided by other departments in the accompanying financial statements.

The Department bills and collects sewer service charges on behalf of the San Francisco Clean Water Program.

(10) Risk Management

The Department is self-insured for general liabilities, property damage and workers' compensation claims. The risk of loss is managed internally by setting aside assets for claim settlement and recording a liability representing an estimate of the cost of all outstanding claims and incurred but not reported claims. Claim liabilities are recorded when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount and, therefore, it is reasonably possible that claim liabilities could change in the future. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and legal factors. The liabilities have been actuarially determined. Changes in the reported liability for the years ended June 30 resulted from the following:

| | 1999 | 1998 |
|--|----------|---------|
| Beginning-of-year liability | \$ 8,189 | 4,741 |
| Current year claims and changes in estimates | 2,140 | 4,803 |
| Current year claims payments | (3,830) | (1,355) |
| End of the year liability | \$ 6,499 | 8,189 |
| General liabilities and property damage | \$ 3,444 | 5,839 |
| Workers' compensation | 3,055 | 2,350 |
| | \$ 6,499 | 8,189 |

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 1999

(With comparative information for June 30, 1998)

(dollars in thousands)

(11) Commitments and Litigation

(a) *Commitments*

As of June 30, 1999, the Department has outstanding commitments with third parties of \$20,979 for various capital projects and other purchase agreements for materials and services.

(b) *Grants*

Grants that the Department receives are subject to audit and final acceptance by the granting agency. Current and prior year costs of such grants are subject to adjustment upon audit.

(c) *Litigation*

The Department is a defendant in various legal actions and claims that arise during the normal course of business, although the final disposition of those legal actions and claims is not determinable. However, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or results of operations of the Department.

(12) Subsequent Events

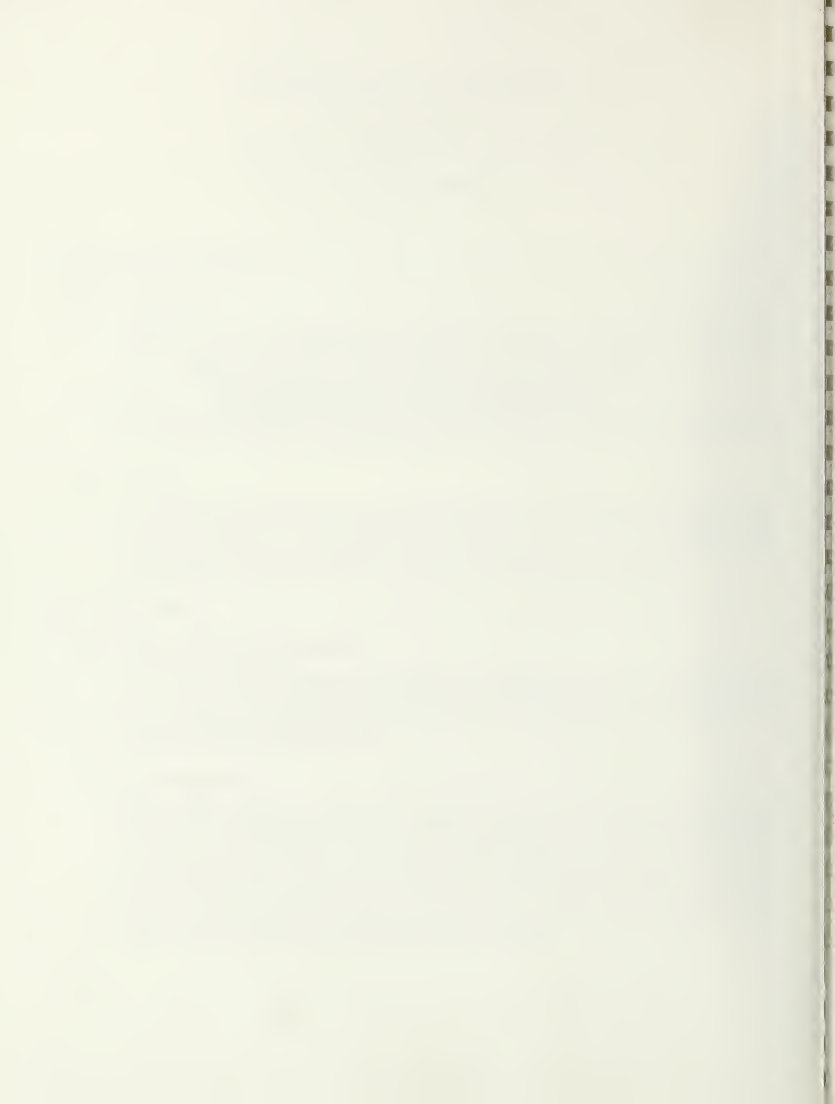
(a) *Issuance of Commercial Paper Notes*

On July 22, 1999, the Department issued \$20,000 of commercial paper notes. Since the date of issuance, interest rates have varied from 2.65% to 3.35% with maturity periods ranging from 4 to 111 days. As of October 22, 1999, the outstanding balance of the commercial paper notes is \$20,000 with maturity dates through January 14, 2000.

(b) *Environmental Issue*

In July 1999, the staff of the California Regional Water Quality Control Board issued a directive instructing the Commission to develop a remedial action plan that addresses environmental contamination located at certain real property owned by the Department. In response to the directive, the Commission is currently in the process of developing such a plan for submission. While the ultimate clean-up cost to be borne by the Department is not currently determinable, it is estimated that the cost would range from \$1,600 to \$11,200, and that the project would be completed over a period of one to five years. Since the ultimate cost of clean-up is not currently determinable, no such amount has been accrued in the accompanying financial statements.

**REQUIRED SUPPLEMENTARY INFORMATION –
YEAR 2000 READINESS INFORMATION**



SAN FRANCISCO WATER DEPARTMENT

Required Supplementary Information

Year 2000 Readiness Information

(unaudited)

(dollars in thousands)

The City is currently addressing Year 2000 issues relating to its computer systems and other electronic equipment. The Year 2000 issue refers to the fact that many computer programs use only the last two digits to refer to a year. Therefore, both 1900 and 2000 would be referred to as "00." Computer programs have to be adjusted to recognize the difference between those two years or the program may fail or create errors. Also, some programs may not be able to recognize that year 2000 is a leap year. Further, the Year 2000 issue could affect electronic equipment containing chips that have date recognition features. The Year 2000 issue may adversely affect the government's operations as early as the fiscal year 1999-2000.

(1) General Description

In 1995, the City began work on Year 2000 issues on a department-by-department basis. In 1998, the City established a central Year 2000 Program Management Office (PMO) expressly for the purpose of providing unified resources and oversight for the City departments' Year 2000 efforts. The PMO has focused City readiness efforts on "mission-critical systems," defined as those services or functions which, if disrupted, would have a direct and immediate impact on a citizen's health, safety or transportation. There are 14 City departments that provide mission critical services to the public.

The mission-critical departments were also instructed to use standardized forms and procedures to report to the PMO. The PMO staff collects the information submitted by departments and reports in turn to the City's Committee on Information Technology Year 2000 Subcommittee, the Board of Supervisors and the Mayor. The PMO also communicates the City's Year 2000 information to the public via the internet, community meetings, and other outreach efforts.

The PMO has assisted departments in conducting inventories and successive steps toward Year 2000 readiness. The PMO's standards have required mission-critical departments to identify those inventory items on which mission-critical systems depend. The PMO has also collected information about systems involving interdepartmental dependencies, where the responsibility for a particular system is not clear. For example, the Police, Fire and Sheriff departments all depend on telecommunications equipment, which is primarily the responsibility of the Department of Telecommunications and Information Services. The PMO has also facilitated the communications between the using departments and the supporting departments to make sure that remediation of particular systems is not delayed while the responsible department is identified, that the responsible department's work is not delayed by repetitive inquiries by multiple user departments, and that a remediation success is translated back to the readiness accounting for each department that uses that system.

Currently, the embedded system program is in the process of independent verification and validation by third party engineers, who are reviewing each step in the mission-critical departments' embedded systems review process and the adequacy of the associated documentation.

In addition, the PMO is currently assisting departments in the ongoing development and refinement of contingency plans. The PMO has provided detailed guidelines and procedures for developing contingency plans, and a uniform format so that the plans can be independently reviewed as part of the PMO's independent verification and validation program.

SAN FRANCISCO WATER DEPARTMENT

Required Supplementary Information

Year 2000 Readiness Information

(unaudited)

(dollars in thousands)

(2) Stages of Work

The City has identified 14 departments that provide mission-critical services to the public. Each department is responsible for performing the following stages of work with respect to the systems and equipment necessary to provide the mission-critical services:

- Awareness stage – Establishing a budget and project plan for dealing with the Year 2000 issue
- Assessment stage – Identifying the systems and components for which Year 2000 compliance work is needed
- Remediation stage – Making changes to systems and equipment
- Validation/testing stage – Validating and testing the changes that were made during the remediation stage

The Commission has completed the awareness and assessment stages for the following mission-critical systems and electronic equipment:

- Water distribution
- Water treatment
- Wastewater collection
- Wastewater treatment
- Power generation
- Power distribution

The remediation and validation/testing stages of the Commission, along with a high-level independent verification and validation by third party engineers through the PMO's office, are scheduled to be completed by November 15, 1999.

(3) Resources Committed

As of year-end, the Commission had outstanding commitments for addressing Year 2000 issues relating to its computer systems and other electronic equipment in the amount of \$235.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. While the City believes that mission-critical systems will function, management cannot assure that the City is or will be Year 2000 ready, that the City's remediation efforts will be successful in whole or in part or that parties with whom the City does business will be Year 2000 ready.

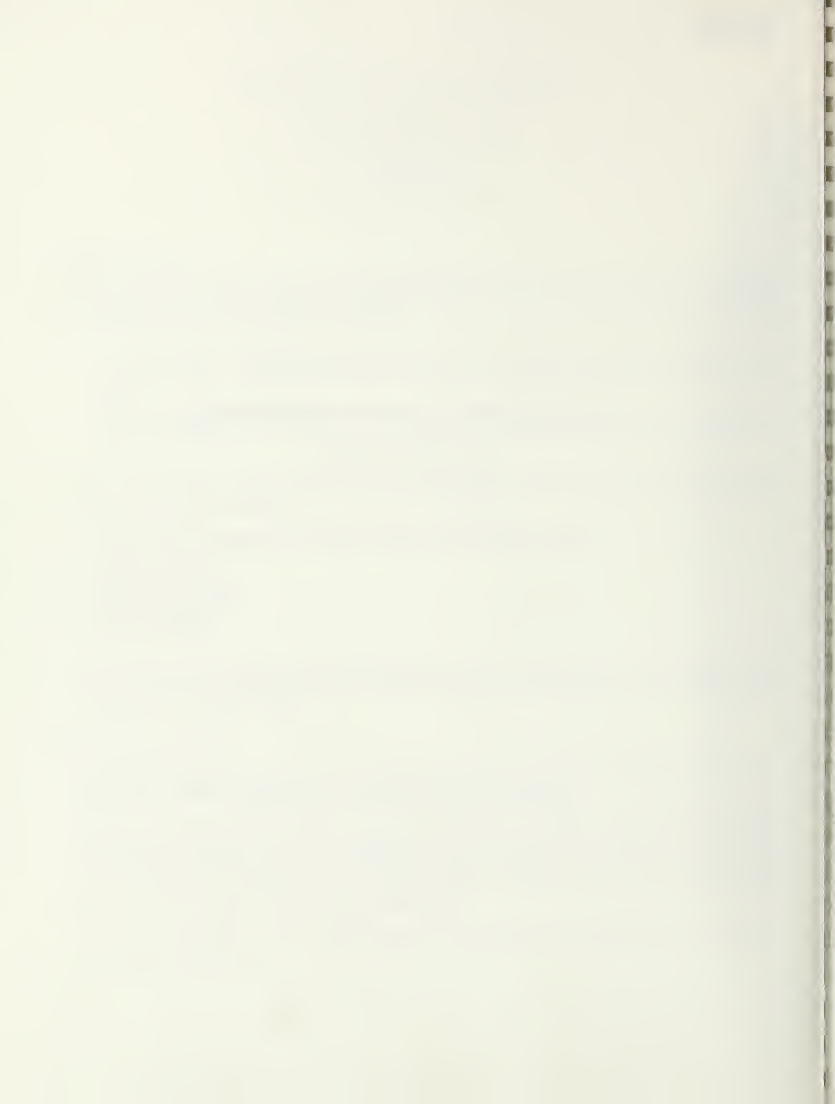
The City's Comprehensive Annual Financial Report provides additional information on how the City is addressing Year 2000 issues.

SAN FRANCISCO CLEAN WATER PROGRAM

Financial Statements

June 30, 1999 and 1998

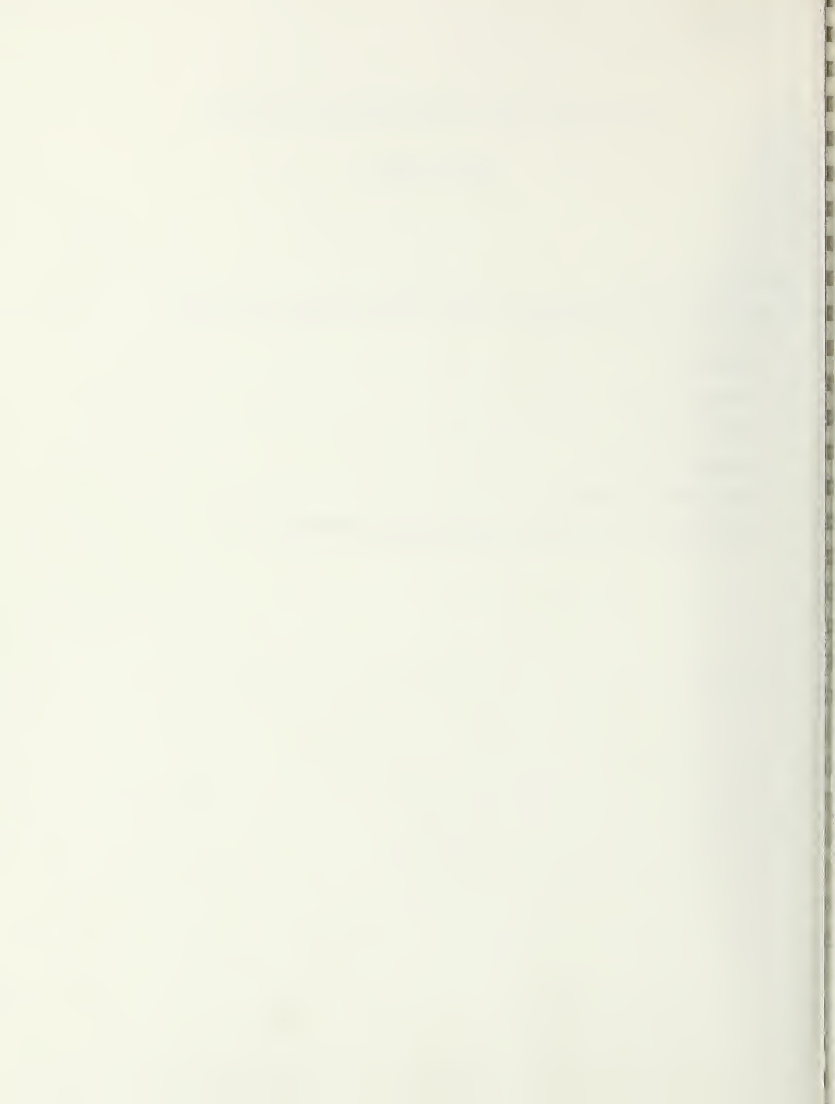
(With Independent Auditors' Report Thereon)



SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

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Independent Auditors' Report

Honorable Mayor and Board of Supervisors
City and County of San Francisco, California:

We have audited the accompanying financial statements of the San Francisco Clean Water Program (the Program) of the City and County of San Francisco, California (the City), as of and for the year ended June 30, 1999, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in note 1, the financial statements present only the Program and are not intended to present fairly the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Francisco Clean Water Program of the City and County of San Francisco, California, as of June 30, 1999, and the results of its operations and its cash flows for the year then ended in conformity with generally accepted accounting principles.

The Year 2000 supplementary information on pages 23 and 24 is not a required part of the financial statements, but is supplementary information required by the Governmental Accounting Standards Board, and we did not audit and do not express an opinion on such information. Further, we were unable to apply to the information certain procedures prescribed by professional standards because of the nature of the subject matter underlying the disclosure requirements and because sufficiently specific criteria regarding the matters to be disclosed have not been established. In addition, we do not provide assurance that the Program is or will become Year 2000 compliant, that the Program's Year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Program does business are or will become Year 2000 compliant.



October 22, 1999



SAN FRANCISCO CLEAN WATER PROGRAM

Balance Sheets

June 30, 1999

(with comparative amounts for June 30, 1998)

(dollars in thousands)

| Assets | 1999 | 1998 |
|---|--------------|-----------|
| Current assets: | | |
| Deposits and investments with City Treasury | \$ 49,006 | 53,445 |
| Receivables: | | |
| Charges for services (net of allowance for doubtful accounts of \$1,500 in 1999 and 1998) | 27,899 | 27,506 |
| Interest and other | — | 1,123 |
| Total receivables | 27,899 | 28,629 |
| Total current assets | 76,905 | 82,074 |
| Restricted assets: | | |
| Deposits and investments with City Treasury | 110,884 | 128,286 |
| Deposits and investments outside City Treasury | 39,570 | 37,726 |
| Interest receivable | 2,022 | 1,074 |
| Total restricted assets | 152,476 | 167,086 |
| Net property, plant and equipment | 1,394,830 | 1,393,561 |
| Bond issuance costs, net of accumulated amortization of \$1,031 in 1999 and \$848 in 1998 | 3,193 | 3,378 |
| Total assets | \$ 1,627,404 | 1,646,099 |
| Liabilities and Equity | | |
| Current liabilities: | | |
| General obligation bonds, current portion | \$ — | 4,660 |
| Revenue bonds, current portion | 20,710 | 18,330 |
| State revolving fund loans, current portion | 11,135 | 10,904 |
| Accounts payable | 1,285 | 1,349 |
| Accrued payroll | 2,117 | 1,903 |
| Accrued vacation, sick leave, and workers' compensation, current portion | 1,362 | 1,225 |
| Bond interest payable | 9,707 | 10,129 |
| Damage and claims liability, current portion | 335 | 6,418 |
| Total current liabilities | 46,651 | 54,918 |
| Liabilities payable from restricted assets | 4,926 | 2,306 |
| Deferred revenue and other long-term liabilities: | | |
| Accrued vacation, sick leave, and workers' compensation | 1,670 | 1,024 |
| Damage and claims liability | 975 | — |
| Deferred revenue | 4,308 | 5,422 |
| Total deferred revenue and other long-term liabilities | 6,953 | 6,446 |
| Long-term debt, less current portion: | | |
| Revenue bonds | 474,063 | 493,158 |
| State revolving fund loans | 156,595 | 167,700 |
| Total long-term debt | 630,658 | 660,858 |
| Total liabilities | 689,188 | 724,528 |
| Equity: | | |
| Contributed capital | 607,964 | 620,683 |
| Retained earnings – reserved for bond requirements and other commitments | 26,959 | 26,365 |
| Retained earnings – unreserved | 303,293 | 274,523 |
| Total equity | 938,216 | 921,571 |
| Total liabilities and equity | \$ 1,627,404 | 1,646,099 |

See accompanying notes to financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM

Statements of Income

Year ended June 30, 1999

(with comparative amounts for the year ended June 30, 1998)
(dollars in thousands)

| | 1999 | 1998 |
|---|------------|----------|
| Operating revenues: | | |
| Charges for services | \$ 142,974 | 140,898 |
| Total operating revenues | 142,974 | 140,898 |
| Operating expenses: | | |
| Personal services | 24,577 | 24,271 |
| Contractual services | 6,346 | 6,084 |
| Materials and supplies | 5,588 | 6,222 |
| Depreciation and amortization | 37,538 | 39,990 |
| General and administrative | 9,808 | 5,893 |
| Services provided by other departments | 20,313 | 21,389 |
| Bad debt expense | 380 | 1,240 |
| Other | 5,329 | 6,844 |
| Total operating expenses | 109,879 | 111,933 |
| Operating income | 33,095 | 28,965 |
| Nonoperating revenues (expenses): | | |
| Operating grant – federal | 822 | 972 |
| Operating grant – state | 15 | 7,766 |
| Interest and investment income | 9,749 | 12,192 |
| Interest expense | (33,241) | (33,358) |
| Other, net | (254) | 735 |
| Net nonoperating expenses | (22,909) | (11,693) |
| Income before operating transfers | 10,186 | 17,272 |
| Operating transfers: | | |
| Operating transfers from the City and County of San Francisco | 4,753 | 4,707 |
| Net income | \$ 14,939 | 21,979 |

See accompanying notes to financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM

Statements of Equity

Year ended June 30, 1999

(with comparative amounts for the year ended June 30, 1998)
(dollars in thousands)

| | Contributed capital | | Contribution from City and County of San Francisco | Retained earnings | Total |
|---|------------------------------|----------------------------|--|----------------------|----------|
| | Federal capital grants | State capital grants | | | |
| Equity at June 30, 1997 | \$ 464,678 | 71,918 | 108,238 | 265,028 | 909,862 |
| Net income | — | — | — | 21,979 | 21,979 |
| Write-off of assets acquired with federal and state capital grants | (8,381) | (1,889) | — | — | (10,270) |
| Allocation of depreciation | (11,975) | (1,906) | — | 13,881 | — |
| Equity at June 30, 1998 | 444,322 | 68,123 | 108,238 | 300,888 | 921,571 |
| Net income | — | — | — | 14,939 | 14,939 |
| Federal and state capital grants, net | 734 | 972 | — | — | 1,706 |
| Allocation of depreciation | (12,495) | (1,930) | — | 14,425 | — |
| Equity at June 30, 1999 | \$ 432,561 | 67,165 | 108,238 | 330,252 | 938,216 |

See accompanying notes to financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM

Statements of Cash Flows

Year ended June 30, 1999

(with comparative amounts for the year ended June 30, 1998)
(dollars in thousands)

| | 1999 | 1998 |
|---|------------|----------|
| Cash flows from operating activities: | | |
| Cash received from customers, including cash deposits | \$ 142,201 | 141,254 |
| Cash paid to employees for services | (24,205) | (23,881) |
| Cash paid to suppliers for goods and services | (15,405) | (12,146) |
| Cash paid for judgments and claims | (6,119) | (1,467) |
| Cash paid for quasi-external transactions | (30,407) | (28,711) |
| Net cash provided by operating activities | 66,065 | 75,049 |
| Cash flows provided by noncapital financing activities – operating grants | 837 | 8,738 |
| Cash flows from capital and related financing activities: | | |
| Capital grants | 1,706 | — |
| State revolving fund loan proceeds | — | 5,000 |
| Transfers from the City for debt service | 4,753 | 4,707 |
| Interest on long-term debt | (33,834) | (35,262) |
| Principal paid on long-term debt | (22,990) | (21,710) |
| Principal paid on loans | (10,874) | (10,317) |
| Acquisition and construction of capital assets | (34,965) | (27,706) |
| Net cash used in capital and related financing activities | (96,204) | (85,288) |
| Cash flows from investing activities: | | |
| Interest income received | 10,472 | 11,581 |
| Proceeds from sale of investments | 51,643 | 86,180 |
| Purchase of investments | (48,912) | (82,036) |
| Other investing activities | 406 | 1,354 |
| Net cash provided by investing activities | 13,609 | 17,079 |
| (Decrease) increase in cash and cash equivalents | (15,693) | 15,578 |
| Cash and cash equivalents: | | |
| Beginning of year | 177,025 | 161,447 |
| End of year | \$ 161,332 | 177,025 |

SAN FRANCISCO CLEAN WATER PROGRAM

Statements of Cash Flows

Year ended June 30, 1999

(with comparative amounts for the year ended June 30, 1998)

(dollars in thousands)

| | 1999 | 1998 |
|--|------------|----------|
| Reconciliation of operating income to net cash provided by operating activities: | | |
| Operating income | \$ 33,095 | 28,965 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | |
| Depreciation and amortization | 37,538 | 39,990 |
| Provision for uncollectible accounts | 380 | 1,240 |
| Other – write-off of fixed assets | — | 5,091 |
| Changes in assets and liabilities: | | |
| Receivables: | | |
| Charges for services, net | (773) | 356 |
| Due from City and County of San Francisco | — | 255 |
| Other | — | 410 |
| Payables: | | |
| Accounts payable | (64) | (189) |
| Accrued payroll | 214 | 66 |
| Accrued vacation, sick leave and workers' compensation | 783 | 47 |
| Damage and claims liability | (5,108) | (1,182) |
| Net cash provided by operating activities | \$ 66,065 | 75,049 |
| Reconciliation of cash and cash equivalents to the balance sheet: | | |
| Deposits and investments with City Treasury: | | |
| Unrestricted | \$ 49,006 | 53,445 |
| Restricted | 110,884 | 128,286 |
| Total deposits and investments | 159,890 | 181,731 |
| Add restricted deposits outside City Treasury meeting the definition of cash equivalents | 1,442 | 796 |
| Less deposits and investments not meeting the definition of cash equivalents | — | (5,502) |
| Cash and cash equivalents at end of year on statements of cash flows | \$ 161,332 | 177,025 |
| Noncash investing, capital and financing activities: | | |
| Write-off of fixed assets | — | (15,296) |
| Depreciation on contributed capital | 14,425 | 13,881 |
| | \$ 14,425 | (1,415) |

See accompanying notes to financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(1) The Financial Reporting Entity

The San Francisco Clean Water Program (the Program) was established in 1977 following the transfer of all sewage-system-related assets and liabilities of the City and County of San Francisco (the City) to the Program on July 1, 1977, which was the first day of the fiscal year in which the San Francisco Series A Sewer Revenue Bonds of 1976 were issued.

In 1976, the electorate of the City approved a proposition authorizing the City to issue \$240,000 in revenue bonds pursuant to the Revenue Bond Law of 1941 of the State of California for the purpose of acquiring, constructing, improving, and financing improvements to the City's municipal sewage treatment and disposal system. Since then, the City's Board of Supervisors has adopted resolutions (the Clean Water Resolutions) providing for the issuance of various sewer revenue and refunding bond series. As of June 30, 1993, the City had exhausted its bonding capacity under the 1976 proposition approved by the electorate. The Clean Water Resolutions require the City to keep separate books of records and accounts of the Program.

The San Francisco Public Utilities Commission (the Commission), established in 1932, is responsible for providing operational oversight of the public utility enterprises of the City, which include the Program along with the City's power and water utilities (e.g., Hetch Hetchy Water and Power [Hetch Hetchy] and the San Francisco Water Department [SFWD]). The Commission consists of five members appointed by the Mayor who are responsible for determining such matters as the rates and charges for services, approval of contracts, and organizational policy. The Commission is a department of the City and, as such, the financial operations of the Program, Hetch Hetchy, and the SFWD are included in the Comprehensive Annual Financial Report of the City as enterprise funds. These financial statements present only the financial operations of the Program and are not intended to present the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types.

(2) Significant Accounting Policies

(a) *Basis of Accounting—Fund Accounting*

The accounts of the Program are organized on the basis of a proprietary fund type, specifically an enterprise fund. The operations of this fund are accounted for with a separate set of self-balancing accounts that comprise the Program's assets, liabilities, fund equity, revenues, and expenses. Enterprise Funds account for operations (a) that are financed and operated in a manner similar to private business enterprises where the intent of the Commission is that the Program's costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or (b) where the Commission has decided that periodic determination of revenues earned, expenses incurred, and net income or loss of the Program is appropriate for capital maintenance, public policy, management control, accountability, or other purpose.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(b) *Measurement Focus*

The financial activities of the Program are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Under this method, all assets and liabilities associated with operations are included on the balance sheet; revenues are recorded when earned and expenses are recorded when liabilities are incurred.

The Program does not apply Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989. The Program applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as statements and interpretations of FASB, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

(c) *Cash and Cash Equivalents*

Cash and cash equivalents include all highly liquid investments, including restricted assets, with an original purchased maturity of three months or less.

(d) *Investments*

Certain investments are stated at fair value based upon quoted market prices. Changes in fair value are recognized as investment income.

Money market funds that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost.

(e) *Property, Plant, and Equipment*

Property, plant, and equipment with an original acquisition date prior to July 1, 1977 are recorded in the financial statements at estimated cost, as determined by an independent professional appraisal, or at cost, if known. All subsequent acquisitions have been recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets which range from 3 to 75 years. No depreciation or amortization is recorded in the year of acquisition and a full year's depreciation or amortization is recorded in the year of disposal.

(f) *Construction in Progress*

The cost of acquisition and construction of major plant and equipment is recorded as construction in progress. As facilities are accepted by the Program and become operative, they are transferred to the plant and equipment accounts and depreciated in accordance with the Program's depreciation policies. Costs of construction projects which are discontinued are recorded as expense in the year in which the decision is made to discontinue the project.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(g) *Capitalization of Interest*

A portion of the interest cost incurred on capital projects is capitalized on assets which require a period of time for construction or to otherwise prepare them for their intended use. Such amounts are amortized over the useful lives of the assets.

(h) *Bond Discount and Issuance Costs*

Bond discount and issuance costs are amortized over the term of the related bonds.

(i) *Accrued Vacation, Sick Leave, and Workers' Compensation*

Accrued vacation pay, which may be accumulated up to ten weeks per employee, is charged to expense as earned. Unused sick leave accumulated through December 6, 1978 is vested and payable upon termination of employment by retirement, death, or disability caused by industrial accident. Sick leave earned subsequent to that date is nonvesting and may be accumulated up to six months per employee. The Program is self-insured for workers' compensation claims and accrues the estimated cost of those claims, including the estimated cost of incurred but not reported claims.

(j) *Damage and Claims Liability*

The Program is self-insured for general liability and property damage claims. The liability represents an estimate of the cost of all outstanding claims, including adverse loss development, and estimated incurred but not reported claims.

(k) *Arbitrage Rebate Payable*

Certain bonds are subject to arbitrage rebate requirements in accordance with regulations issued by the U.S. Treasury Department. The requirements generally stipulate that earnings from the investment of the tax-exempt bond proceeds that exceed related interest costs on the bonds must be remitted to the federal government on every fifth anniversary of each bond issue. There was no arbitrage rebate liability as of June 30, 1999 and 1998.

(l) *Refunding of Debt*

Gains or losses occurring from advance refundings of debt are deferred and amortized into interest expense over the remaining life of the old bonds or the life of the new bonds, whichever is shorter.

(m) *Income Taxes*

As a government agency, the Program is exempt from both federal income taxes and California state franchise taxes.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(n) Contribution from the City and County of San Francisco

The net book value of all assets and liabilities, including liabilities under sewage-related general obligation bonds relating to the sewage system transferred from the City to the Program, are reflected as contributed capital in the accompanying financial statements.

(o) Revenue Recognition

Sewer service charges are based on water usage as determined by the SFWD. Billings are on a monthly or bimonthly basis. Revenues reflected in the financial statements include accruals based on estimates for the periods between termination of the billing cycle and the end of the fiscal year.

Sewer revenue rates must be set to produce sufficient revenue to fund the obligations of the Program as defined in the Clean Water Resolutions, including costs for operation, maintenance, repair and replacements, revenue bond debt service and compliance with federal and state laws and regulations. In addition, City Ordinance No. 198-77 requires that rates be recommended annually to produce sufficient revenue (except to the extent that funds are provided by transfers from other City funds – note 10) to pay debt service on sewage-related general obligation bonds (note 6).

In June 1998, the voters passed Proposition H, which effectively froze the sewer rates at the levels in effect as of January 1, 1998 until July 1, 2006, subject to certain exceptions such as to service pre-existing debt. The passage of Proposition H limits the Program's ability to fund future sewer maintenance projects and/or meet new federal or state regulations that may arise during the period in which Proposition H is effective.

(p) Contributed Capital

The Program receives federal and state grants for the purpose of acquisition or construction of property and equipment. These grants are recorded as contributed capital when the grant is earned. Grants are generally earned upon expenditure of funds. The gross amount of depreciation is presented as an expense in the statements of income with the portion of depreciation relating to assets acquired with capital grants being added back after net income and closed to contributed capital.

(q) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(r) Reclassifications

Certain reclassifications have been made to the 1998 financial statements to conform to the 1999 presentation. These reclassifications did not change total assets, liabilities, equity or net income.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(3) Cash and Investments

The captions on the balance sheet related to cash and investments at June 30 are as follows:

| | <u>1999</u> | <u>1998</u> |
|---|-------------------|----------------|
| Deposits and investments with City Treasury: | | |
| Unrestricted – pooled | \$ 49,006 | 53,445 |
| Restricted – pooled and nonpooled (note 5) | 110,884 | 128,286 |
| Deposits and investments outside City Treasury – restricted (note 5) | <u>39,570</u> | <u>37,726</u> |
| | <u>\$ 199,460</u> | <u>219,457</u> |

Investments

The Program's deposits and investments with the City Treasury are invested pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy guidelines are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The City's Comprehensive Annual Financial Report categorizes the level of custodial risk associated with its pooled cash and investments, which includes \$155,905 and \$177,863 of the Program's total deposits and investments with the City Treasury as of June 30, 1999 and 1998, respectively. The City Treasury allocates monthly income from the investment of pooled cash in proportion to the Program's end-of-month balances.

The Program is required by its bond indentures to maintain certain revenue bond funds in government obligations, time deposits, or demand deposits. The Program follows the investment policy guidelines of the City Treasurer for its other investments, including those investments held by trustees.

The Program's investments, including those held by trustees, are categorized below to give an indication of the level of custodial risk assumed at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the Program or its agent in the name of the Program. Category 2 includes uninsured and unregistered investments for which the securities are held by the counter-party's trust department or agent in the name of the Program. Category 3 includes uninsured and unregistered investments for which the securities are held by the counter-party, or by its trust department or agent but not in the name of the Program.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

The Program's investment portfolio is stated at fair value (except for money market funds which are stated at amortized cost, which approximates market) and is based on quotes obtained from national exchanges as of June 30, 1999.

| | Category | | | Carrying value |
|---|------------------|----------|----------|-------------------|
| | 1 | 2 | 3 | |
| U.S. Treasury bills | \$ 25,440 | — | — | 25,440 |
| Other U.S. government securities | 16,673 | — | — | 16,673 |
| | <u>\$ 42,113</u> | <u>—</u> | <u>—</u> | 42,113 |
| Money market funds | | | | 1,442 |
| Pooled cash and investments held by the City Treasurer | | | | <u>155,905</u> |
| | | | | <u>\$ 199,460</u> |

(4) Property, Plant, and Equipment

Property, plant, and equipment at June 30 consisted of the following:

| | 1999 | 1998 |
|--|---------------------|------------------|
| Land | \$ 22,192 | 22,192 |
| Buildings, structures and improvements | 1,837,875 | 1,782,091 |
| Equipment | 18,224 | 17,761 |
| Construction-in-progress | <u>8,805</u> | <u>26,245</u> |
| | 1,887,096 | 1,848,289 |
| Less accumulated depreciation and amortization | <u>(492,266)</u> | <u>(454,728)</u> |
| | <u>\$ 1,394,830</u> | <u>1,393,561</u> |

During the years ended June 30, 1999 and 1998, the Program incurred total interest cost of \$34,549 and \$35,922, respectively. Of the total amount of interest cost incurred, \$1,308 and \$2,564 was capitalized into the cost of constructed assets during the years ended June 30, 1999 and 1998, respectively.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

During fiscal year 1998, the Program wrote off fixed assets totaling approximately \$15.3 million. Included in the amount written off was approximately \$13.8 million relating to the cross-town tunnel project which would have connected the Bayside and Oceanside Sewage Treatment Plants. This project was originally initiated as a result of the cease and desist order issued by the Environmental Protection Agency (EPA); however, during fiscal year 1998 the EPA amended the original cease and desist order which eliminated the need for the completion of the project. The remaining \$1.5 million of write-offs pertained to design and planning costs on certain projects which were discontinued during fiscal year 1998. Of the amount written-off, \$10.3 million were assets acquired by capital grant funding which resulted in a reduction of contributed capital. The remaining \$5 million was recognized as other operating expenses in the accompanying financial statements.

During fiscal year 1999, the Program expensed approximately \$3.3 million related to capitalized design and planning costs on certain projects which were discontinued during fiscal year 1999. The amount of the write-off was recognized as other operating expense in the accompanying financial statements.

(5) Restricted Assets

Pursuant to the Clean Water Resolutions, all revenue of the Program (except amounts on deposit in the rebate fund) are irrevocably pledged to the punctual payment of debt service on the Sewer Revenue and Refunding Bonds. Accordingly, the revenue of the Program shall not be used for any other purpose while any of its Sewer Revenue and Refunding Bonds are outstanding except as expressly permitted by the Clean Water Resolutions. Further, all revenues shall be deposited by the City Treasurer in special funds designated as the Sewer Service Revenue Fund (the Sewer Revenue Fund), which must be maintained in the City Treasury. Deposits in the Sewer Revenue Fund, including earnings thereon, shall be appropriated, transferred, expended, or used for the following purposes pertaining to the financing, maintenance and operation of the Program in accordance with the following priority:

1. The payment of State loans.
2. The payment of maintenance and operation costs of the Program.
3. The payment of fees and expenses of the Fiscal Agent and payment of the periodic fees, if any, payable to any Reserve Provider or Credit Provider in conjunction with the Bonds.
4. The payment of amounts required to be deposited into the Principal Fund, Interest Fund, Bond Reserve Fund, Sinking Fund Accounts, and any other mandatory funds and accounts created to secure Bonds issued by the City for the financing or the refinancing of the acquisition, construction or extension of the Program.
5. The payment of, or deposit into, the debt service, reserve and other mandatory funds and accounts created to secure obligations of the City payable from net revenues for the financing or refinancing of the Program which are subordinated to the Bonds.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

6. Any deposits required to be made into the Repair and Replacement Fund pursuant to the Clean Water Resolutions.
7. Any deposit to be made into the Working Capital Fund pursuant to the Clean Water Resolutions.
8. Any deposit to be made into the Rate Stabilization Fund pursuant to the Clean Water Resolutions.
9. Any deposit to be made into the Surplus Revenue Fund pursuant to the Clean Water Resolutions.

In accordance with the Clean Water Resolutions, the Program maintains certain restricted cash and investment balances in trust. Restricted assets held in trust consisted on the following at June 30:

| | <u>1999</u> | <u>1998</u> |
|---|--------------------------|-----------------------|
| Equity in deposits and investments of the City Treasurer: | | |
| Sewer Bond Construction Fund | \$ <u>110,884</u> | <u>128,286</u> |
| Total | <u>110,884</u> | <u>128,286</u> |
| Investments held by trustee: | | |
| 1991 Sewer Revenue Bond Fund | 2,885 | 2,778 |
| 1992 Sewer Revenue Refunding Bond Fund | 19,385 | 18,783 |
| 1994 Sewer Revenue Refunding Bond Fund | 15,858 | 15,369 |
| 1995 Sewer Revenue Bond Fund | <u>1,442</u> | <u>796</u> |
| Total | <u>39,570</u> | <u>37,726</u> |
| Interest receivable: | | |
| Sewer Bond Construction Fund | <u>2,022</u> | <u>1,074</u> |
| Total | <u>2,022</u> | <u>1,074</u> |
| Total restricted assets | \$ <u><u>152,476</u></u> | <u><u>167,086</u></u> |

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(6) Long-Term Debt

Long-term debt consisted of the following at June 30:

| | Interest rates | Due serially to | 1999 | 1998 |
|--|-------------------|--------------------|------------|----------|
| General obligation bonds: | | | | |
| 1970 Water Pollution Control Bonds – Series D | 4%–6% | 1999 | \$ — | 2,770 |
| 1972 Sewer System Improvement Bonds – Series C | 4%–6% | 1999 | — | 1,890 |
| Total general obligation bonds | | | — | 4,660 |
| Less current portion of general obligation bonds | | | — | (4,660) |
| Long-term portion of general obligation bonds | | | \$ — | — |
| Revenue Bonds: | | | | |
| 1991 Sewer Revenue Bonds | 5.75%–6.5% | 2003 | 12,980 | 15,750 |
| 1992 Sewer Revenue Refunding Bonds | 5.5%–6% | 2016 | 264,820 | 280,380 |
| 1994 Sewer Revenue Refunding Bonds | 4.7%–5.8% | 2023 | 174,980 | 174,980 |
| 1995A Sewer Revenue Bonds | 5.38%–5.95% | 2026 | 44,230 | 44,230 |
| 1995B Sewer Revenue Bonds | 5.55%–5.95% | 2011 | 14,157 | 13,376 |
| Unamortized bond discount and refunding loss | | | (16,394) | (17,228) |
| Total revenue bonds | | | 494,773 | 511,488 |
| Less current portion of revenue bonds | | | (20,710) | (18,330) |
| Long-term portion of revenue bonds | | | \$ 474,063 | 493,158 |

The payments of principal and interest amounts on various bonds are collateralized by future sewer and water revenues.

(a) General Obligation Bonds

Pursuant to City policy, the Program was obligated to pay the principal and interest of General Obligation Bonds of the City that relate to sewage and water pollution control. The bonds had interest rates that range from 4% to 6% and matured annually through fiscal year 1999.

The Program has complied with the debt covenants of the General Obligation Bonds.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(b) General Purpose Sewer Revenue Bonds Series 1991

In July 1991, the Board of Supervisors of the City adopted resolutions providing for the issuance of \$170,000 General Purpose Sewer Revenue Bonds (Series 1991). Interest rates for the issue vary from 5.75% to 6.5%.

The Series 1991 Bonds did not require voter approval as the bonds were to be used to finance facilities under Cease and Desist Orders from the San Francisco Bay Regional Water Quality Control Board (the Regional Board). The bonds are payable solely from pledged revenues of the Program and are not payable from any other source.

On March 2, 1994 Sewer Revenue Refunding Bonds Series 1994 were issued with a face value of approximately \$175,000 of which net proceeds were used to refund approximately \$144,700 of the Series 1991 Bonds in a legal defeasance (note 6d).

(c) Sewer Revenue Refunding Bonds Series 1992

On August 4, 1992, the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Refunding Bonds Series 1992 (the 1992 Refunding Bonds) in the principal amount of approximately \$331,000 with interest rates varying from 5.5% to 6% maturing serially through October 1, 2015.

(d) Sewer Revenue Refunding Bonds Series 1994

On January 24, 1994, the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Refunding Bonds Series 1994 (the 1994 Refunding Bonds) in the principal amount of \$174,980 with interest rates varying from 4.7% to 5.38%. Interest-only payments are due semi-annually on April 1 and October 1 of each year until April 1, 2000, at which time the bonds begin to mature serially through October 1, 2022.

(e) Sewer Revenue Bonds, Series 1995

On November 8, 1994, voters approved the issuance of Sewer Revenue Bonds in the amount of approximately \$146,100. On May 8, 1995 the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Bonds Series 1995A and 1995B (the 1995 Bonds). The Series 1995A Bonds have a principal amount of approximately \$44,200 with interest varying from 5.38% to 5.95% and mature serially through October 1, 2025. Interest payments are due semiannually on April 1 and October 1 of each year. The Series 1995B Bonds have a principal amount of approximately \$11,300 with interest varying from 5.55% to 5.95% and mature serially from October 1, 2006 through October 1, 2010. Interest payments are due semi-annually beginning October 1, 2006 through October 1, 2010. The Program recognizes annual interest expense on the Series 1995B Bonds over the life of the Bonds using the interest method. The Program has recognized approximately \$2,900 and \$2,100 of unpaid interest on the Series 1995B Bonds at June 30, 1999 and 1998, respectively, and has included it with the outstanding principal balance of

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

the Series 1995B Bonds. The Series Revenue Bonds were issued for the purpose of providing funds for certain improvements to the City's sewage treatment and disposal system.

(f) *Future Annual Debt Service of Revenue Bonds*

The future annual debt service relating to the Revenue Bonds outstanding at June 30, 1999 is as follows:

| | <u>Principal</u> | <u>Interest</u> |
|--|--------------------------|--------------------------|
| Year ending June 30: | | |
| 2000 | \$ 20,710 | 27,801 |
| 2001 | 22,275 | 26,659 |
| 2002 | 23,555 | 25,442 |
| 2003 | 24,930 | 24,153 |
| 2004 | 20,415 | 22,970 |
| Thereafter | <u>399,282</u> | <u>191,436</u> |
| | 511,167 | \$ <u><u>318,461</u></u> |
| Less: | | |
| Current portion | (20,710) | |
| Unamortized bond discount and refunding loss | <u>(16,394)</u> | |
| Long-term portion at June 30, 1999 | \$ <u><u>474,063</u></u> | |

As defined in the Clean Water Resolutions, the principal and interest of the Program's Revenue and Refunding Bonds are payable from its corresponding revenue as well as monies deposited in certain funds and accounts pledged thereto (note 5).

The Program has complied with the debt covenants of the Revenue Bonds.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(7) State Revolving Fund Loans

The Program maintains several contracts with the California State Water Resources Board (SWRCB) under which the Program can borrow up to prescribed maximum amounts to finance the construction of certain facilities. Loans outstanding at June 30, 1999 are summarized as follows:

| Project | Date of loan | Maturity date | Interest rate | Amount outstanding | Maximum loan amount |
|--------------|--------------|---------------|---------------|--------------------|---------------------|
| Oceanside | 07/25/90 | 2010 | 3.4% | \$ 26,742 | 40,000 |
| Oceanside | 06/10/91 | 2011 | 3.5% | 21,647 | 32,376 |
| Mariposa | 01/10/91 | 2011 | 3.5% | 5,133 | 7,624 |
| Oceanside | 04/28/92 | 2007 | 3.5% | 24,933 | 42,200 |
| Mariposa | 11/01/91 | 2011 | 3.1% | 1,388 | 1,936 |
| Lake Merced | 02/05/92 | 2012 | 3.1% | 15,112 | 21,114 |
| Islais Creek | 10/08/92 | 2012 | 3.0% | 4,304 | 5,706 |
| Oceanside | 12/24/93 | 2012 | 2.9% | 11,376 | 14,100 |
| Islais Creek | 09/07/93 | 2012 | 3.1% | 21,415 | 26,800 |
| Islais Creek | 06/17/94 | 2013 | 2.9% | 12,909 | 15,000 |
| Islais Creek | 06/13/96 | 2015 | 3.4% | 8,910 | 10,000 |
| Rankin Pump | 12/23/96 | 2017 | 3.1% | 13,861 | 15,000 |
| | | | | <u>\$ 167,730</u> | <u>231,856</u> |

The Program is repaying the interest and principal by installments with the final amount due from 15 to 20 years after the first disbursement by SWRCB. Disbursements are made by SWRCB as funds are spent for the projects. The Program is required to comply with applicable federal and state regulations. The future annual debt service relating to the State Revolving Fund Loans outstanding at June 30, 1999 is as follows:

| | Principal | Interest |
|------------------------------------|-------------------|------------------|
| Year ending June 30: | | |
| 2000 | \$ 11,135 | 5,419 |
| 2001 | 11,501 | 5,053 |
| 2002 | 11,879 | 4,676 |
| 2003 | 12,270 | 4,285 |
| 2004 | 12,672 | 3,882 |
| Thereafter | <u>108,273</u> | <u>17,199</u> |
| | 167,730 | <u>\$ 40,514</u> |
| Less current portion | <u>(11,135)</u> | |
| Long-term portion at June 30, 1999 | <u>\$ 156,595</u> | |

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(8) **Deferred Revenue**

In January 1995, the Program entered into a forward purchase and sale agreement with an investment bank (the Bank). Under the agreement, the Program received an upfront fee of approximately \$8,900 from the Bank. In exchange, the Program will use its debt service payments deposited but not yet due to bondholders to purchase short-term U.S. Treasury bills from the Bank at face value.

The upfront fee was deposited into the Program's Rate Stabilization Fund and recorded as deferred revenue in the accompanying financial statements. Revenue is being recognized over the life of the agreement based on the present value of the future earnings. The unamortized balance at June 30, 1999 and 1998 is approximately \$4,300 and \$5,400, respectively.

(9) **Employee Benefits**

(a) ***Retirement Plan***

Plan Description—The City has a single-employer defined benefit retirement plan (the Plan) which is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). The Plan covers substantially all full-time employees of the Program along with other employees of the City. The Plan provides basic service retirement, disability and death benefits based on specified percentages of final average salary and provides cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City and County Employees' Retirement System, 1155 Market Street, 2nd Floor, San Francisco, CA 94103 or by calling (415) 554-1520.

Funding Policy—Contributions are made to the basic plan by both the Program and employees. Employee contributions are mandatory. Employee contribution rates for 1999 and 1998 varied from 7% to 8% as a percentage of covered salary. The Program is required to contribute at an actuarially determined rate. No Program contributions were required for 1999 and 1998 as the actuarially determined contribution rate as a percentage of covered payroll was 0%. The Program's contributions to the Retirement System on behalf of its employees amounted to \$1,336, \$1,201 and \$857 for the years ended June 30, 1999, 1998, and 1997, respectively, which was equal to the required employee contributions for those years.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

(b) *Health Care Benefits*

Health care benefits of Program employees, retired employees and surviving spouses are financed by beneficiaries and the City through the City and County of San Francisco Health Service System, an internal service fund. The Program's contributions covering current and retired employees, which amounted to approximately \$1,300 and \$1,200 in fiscal years 1999 and 1998, respectively, is determined by Charter provisions based on similar contributions made by the ten most populous counties in California. The Program's liability for both current employee and postretirement health care benefits is limited to its annual contribution.

(10) **Related Parties**

Certain administrative costs of the Commission are allocated to the Program. For the years ended June 30, 1999 and 1998, the Commission allocated \$9,283 and \$5,218, respectively, in administrative costs to the Program, which are included in general and administrative expenses in the accompanying financial statements.

The City performs certain administrative services such as maintenance of accounting records and investment of cash for all fund groups within the City. The various funds are charged for these services based on the City's indirect cost allocation plan. The overhead allocation paid to the General Fund of the City by the Program was \$1,735 and \$1,679 for the years ended June 30, 1999 and 1998, respectively, and is included in other operating expenses in the accompanying financial statements.

The City transferred \$4,753 and \$4,707 from its Debt Service Fund to the Program during the years ended June 30, 1999 and 1998, respectively, to provide for general obligation bond debt service of the Program.

The Program purchases electricity from the Hetch Hetchy Project at market rates. This amount, totaling \$5,701 and \$6,396 for the years ended June 30, 1999 and 1998, respectively, has been included in services provided by other departments in the accompanying financial statements.

The Program provides sewer services to other City departments at the nonresidential rates established by the Program.

The SFWD bills and collects sewer service charges on behalf of the Program.

The City's Department of Public Works (DPW) provides certain engineering and other services to the Program and charges amounts designed to recover its costs. This amount totaling approximately \$10,500 and \$10,000 for the years ended June 30, 1999 and 1998, respectively, has been included in services provided by other departments in the accompanying financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

A variety of other City departments provides services such as purchasing, legal, data processing, telecommunications and human resources to the Program and charge amounts designed to recover those departments' costs. These charges totaling approximately \$4,100 and \$2,800 for the years ended June 30, 1999 and 1998, respectively, have been included in services provided by other departments in the accompanying financial statements.

(11) Risk Management

The Program is self-insured for general liabilities, property damage and workers' compensation claims. The risk of loss is managed internally by setting aside assets for claim settlement and recording a liability representing an estimate of the cost of all outstanding claims and incurred but not reported claims. Claim liabilities are recorded when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount and, therefore, it is reasonably possible that claim liabilities could change in the future. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and legal factors. The liabilities have been actuarially determined. Changes in the reported liability for the years ended June 30, 1999 and 1998 resulted from the following:

| | <u>1999</u> | <u>1998</u> |
|--|-----------------|----------------|
| Beginning of year liability | \$ 6,925 | 8,143 |
| Current year claims and changes in estimates | 1,637 | 249 |
| Current year claims payments | <u>(6,119)</u> | <u>(1,467)</u> |
| End of the year liability | <u>\$ 2,443</u> | <u>6,925</u> |
| General liabilities and property damage | 1,310 | 6,418 |
| Workers' compensation | <u>1,133</u> | <u>507</u> |
| | <u>\$ 2,443</u> | <u>6,925</u> |

(12) Commitments, Litigation and Contingencies

(a) Commitments

As of June 30, 1999, the Program has outstanding commitments with third parties of \$14,700 for various capital projects and other purchase agreements for materials and services.

(b) Grants

Grants that the Program receives are subject to audit and final acceptance by the granting agency. Current and prior year costs of such grants are subject to adjustment upon audit.

SAN FRANCISCO CLEAN WATER PROGRAM FUND GROUP

Notes to Financial Statements

June 30, 1999

(with comparative information for June 30, 1998)

(dollars in thousands)

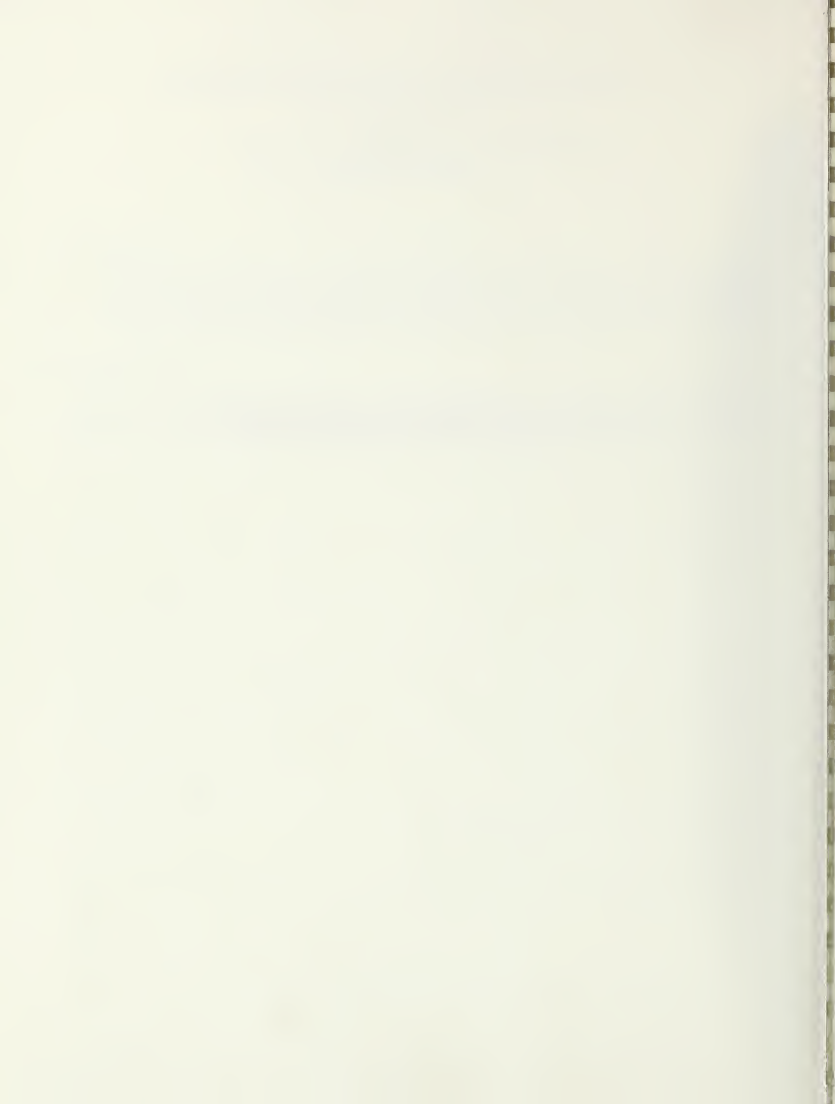
(c) *Litigation*

The Program is a defendant in various legal actions and claims that arise during the normal course of business, although the final disposition of these legal actions and claims is not determinable. However, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or results of operations of the Program.

(13) **Subsequent Event**

In July 1999, the City's Board of Supervisors authorized the Commission to apply for and enter into loan agreements not to exceed \$50,000 with the State of California for the purpose of providing funding for prior expenditures incurred in the construction of the Islais Creek/Rankin Street storage facilities.

**REQUIRED SUPPLEMENTARY INFORMATION –
YEAR 2000 READINESS INFORMATION**



SAN FRANCISCO CLEAN WATER PROGRAM

Required Supplementary Information

Year 2000 Readiness Information (unaudited) (dollars in thousands)

The City is currently addressing Year 2000 issues relating to its computer systems and other electronic equipment. The Year 2000 issue refers to the fact that many computer programs use only the last two digits to refer to a year. Therefore, both 1900 and 2000 would be referred to as "00." Computer programs have to be adjusted to recognize the difference between those two years or the program may fail or create errors. Also, some programs may not be able to recognize that year 2000 is a leap year. Further, the Year 2000 issue could affect electronic equipment containing chips that have date recognition features. The Year 2000 issue may adversely affect the government's operations as early as the fiscal year 1999-2000.

(1) General Description

In 1995, the City began work on Year 2000 issues on a department-by-department basis. In 1998, the City established a central Year 2000 Program Management Office (PMO) expressly for the purpose of providing unified resources and oversight for the City departments' Year 2000 efforts. The PMO has focused City readiness efforts on "mission-critical systems," defined as those services or functions which, if disrupted, would have a direct and immediate impact on a citizen's health, safety or transportation. There are 14 City departments that provide mission critical services to the public.

The mission-critical departments were also instructed to use the standardized forms and procedures to report to the PMO. The PMO staff collects the information submitted by departments and reports in turn to the City's Committee on Information Technology Year 2000 Subcommittee, the Board of Supervisors and the Mayor. The PMO also communicates the City's Year 2000 information to the public via the Internet, community meetings, and other outreach efforts.

The PMO has assisted departments in conducting inventories and successive steps toward Year 2000 readiness. The PMO's standards have required mission-critical departments to identify those inventory items on which mission-critical systems depend. The PMO has also collected information about systems involving interdepartmental dependencies, where the responsibility for a particular system is not clear. For example, the Police, Fire and Sheriff departments all depend on telecommunications equipment, which is primarily the responsibility of the Department of Telecommunications and Information Services. The PMO has also facilitated the communications between the using departments and the supporting departments to make sure that remediation of particular systems is not delayed while the responsible department is identified, that the responsible department's work is not delayed by repetitive inquiries by multiple user departments, and that a remediation success is translated back to the readiness accounting for each department that uses that system.

Currently, the embedded system program is in the process of independent verification and validation by third party engineers, who are reviewing each step in the mission-critical departments' embedded systems review process and the adequacy of the associated documentation.

SAN FRANCISCO CLEAN WATER PROGRAM

Required Supplementary Information

Year 2000 Readiness Information (unaudited) (dollars in thousands)

In addition, the PMO is currently assisting departments in the ongoing development and refinement of contingency plans. The PMO has provided detailed guidelines and procedures for developing contingency plans, and a uniform format so that the plans can be independently reviewed as part of the PMO's independent verification and validation program.

(2) Stages of Work

The City has identified 14 departments that provide mission-critical services to the public. Each department is responsible for performing the following stages of work with respect to the systems and equipment necessary to provide the mission-critical services:

- Awareness stage – Establishing a budget and project plan for dealing with the Year 2000 issue
- Assessment stage – Identifying the systems and components for which Year 2000 compliance work is needed
- Remediation stage – Making changes to systems and equipment
- Validation/testing stage – Validating and testing the changes that were made during the remediation stage

The Commission has completed the awareness and assessment stages for the following mission-critical systems and electronic equipment:

- Water distribution
- Water treatment
- Wastewater collection
- Wastewater treatment
- Power generation
- Power distribution

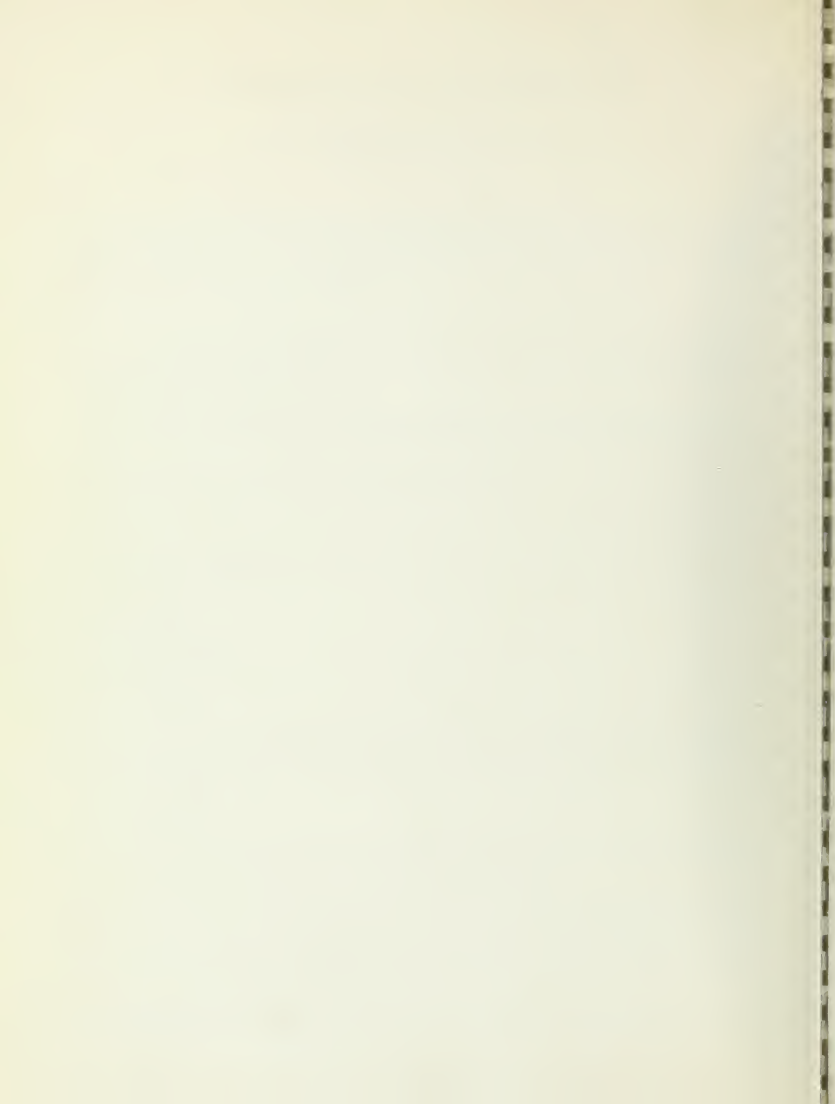
The remediation and validation/testing stages of the Commission, along with a high-level independent verification and validation by third party engineers through the PMO's office, are scheduled to be completed by November 15, 1999.

(3) Resources Committed

As of year-end, the Commission had outstanding commitments for addressing Year 2000 issues relating to its computer systems and other electronic equipment in the amount of \$235.

Because of the unprecedented nature of the Year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the Year 2000 and thereafter. While the City believes that mission-critical systems will function, management cannot assure that the City is or will be Year 2000 ready, that the City's remediation efforts will be successful in whole or in part or that parties with whom the City does business will be Year 2000 ready.

The City's Comprehensive Annual Financial Report provides additional information on how the City is addressing Year 2000 issues.

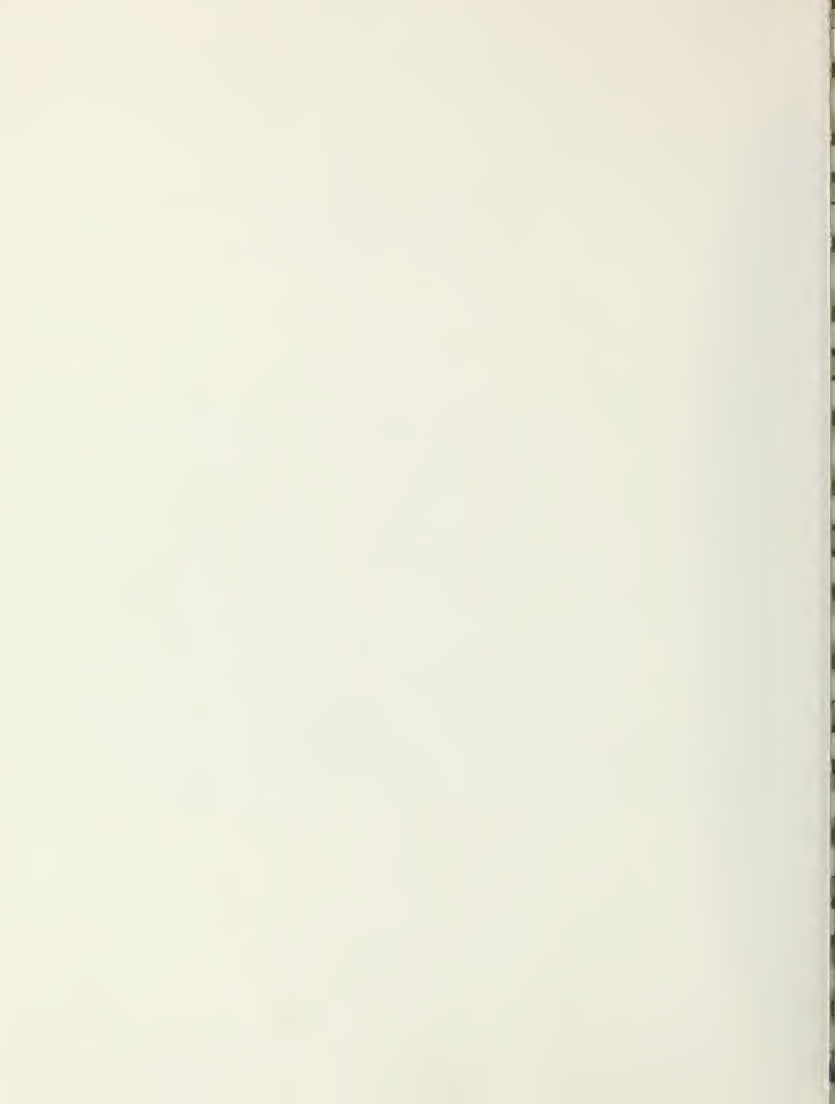


SAN FRANCISCO PUBLIC UTILITIES COMMISSION



Annual Report 1999-2000

San Francisco, California
For the Year Ended June 30, 2000





December 15, 2000

Honorable Mayor Willie L. Brown, Jr.
Honorable Members of the Board of Supervisors
City and County of San Francisco
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102

Dear Mayor Brown and Members of the Board:

In compliance with Section 4.103 of the City Charter, I am privileged to provide you with the San Francisco Public Utilities Commission's Annual Report for the Fiscal Year 1999-2000.

This year's successes included cutting operating costs further, creating more efficient processes for planning, contracting and program management, maximizing the values of our real estate and other tangible property, as well as strengthening ties with representatives of our vast service areas that stretch beyond the boundaries of our City and County.

We remained focused on our goals of increasing our existing water supplies by at least 30 percent, maintaining the filtration exemption for the Hetch Hetchy supply, weighing the health needs of our customers and our stewardship of the environment against demands for access to our watersheds and — most importantly — preparing for the seismic retrofitting and updating of our aging facilities at projected costs that run into the billions. Financing such a large capital improvement program is a major challenge, because San Francisco ratepayers cannot carry the full cost.

In the past twelve months, we have had to fill key management positions, streamline our operations, and address serious declines in our power revenues caused by deregulation and restrictions on sales to private entities.

The challenges, although daunting, have also provided us with opportunities: to craft a stronger organizational structure, to evolve new ways of doing business and raising revenues, and to reach out in better fashion to all our constituents and stakeholders so as to arrive at broader-based solutions. Through it all, our very best assets remain the men and women of the San Francisco Public Utilities Commission.

Sincerely,

E. Dennis Normandy
President

DOCUMENTS DEPT.

FEB 20 2001

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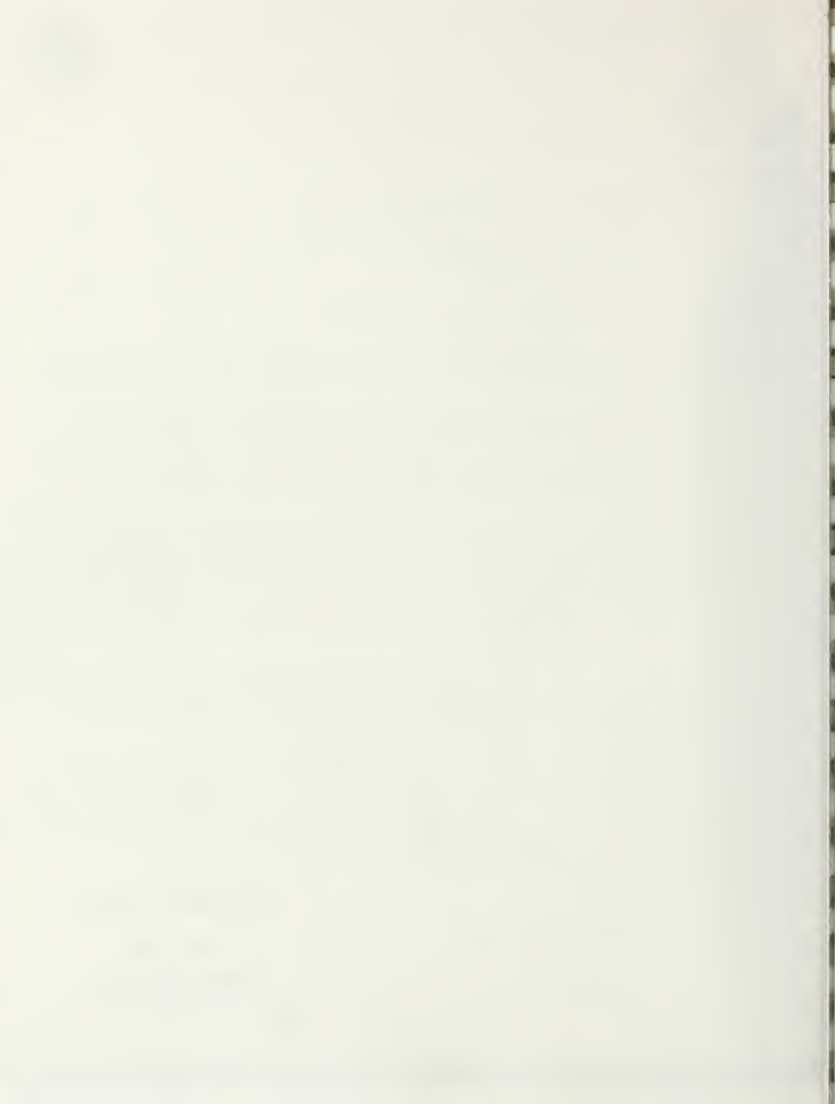


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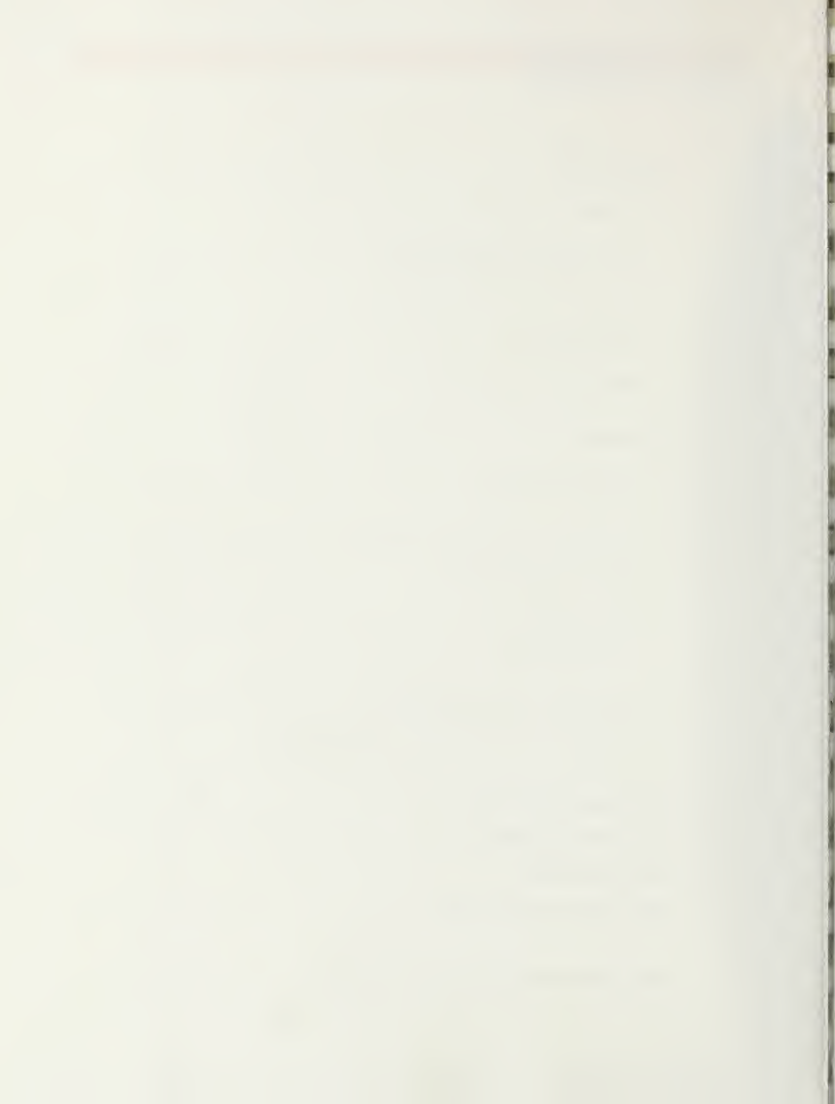
PUC FINANCIAL STATEMENTS

CLEAN WATER PROGRAM

WATER DEPARTMENT

HETCH HETCHY WATER & POWER

Photos of Watershed Keeper courtesy of Lionel Da Silva



SAN FRANCISCO PUBLIC UTILITIES COMMISSION MISSION

To serve San Francisco and its Bay Area customers with reliable, high quality and affordable water, while maximizing benefits from power operations and responsibly managing the resources entrusted to its care.

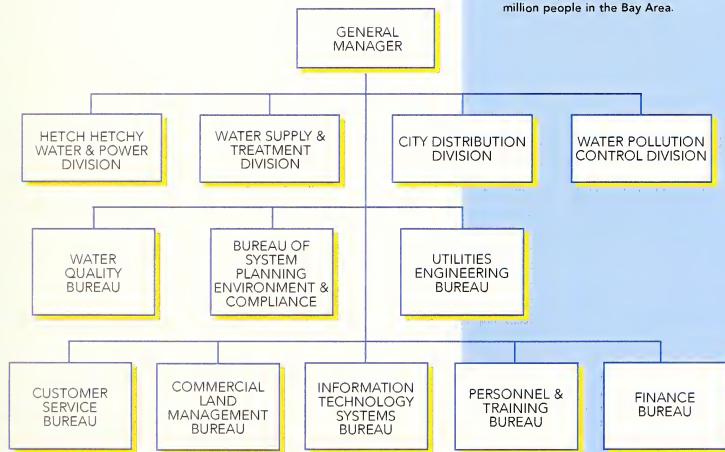
To protect public health and the aquatic environment by providing safe, reliable and efficient collection, treatment and disposal of San Francisco's wastewater.

To conduct its business affairs in a manner that promotes efficiency, minimizes waste and assures rate-payer confidence.

To promote diversity and the health, safety and professional development of its employees.



Hetch Hetchy reservoir near Yosemite provides water for 2.4 million people in the Bay Area.



INTRODUCTION

The San Francisco Public Utilities Commission (SFPUC) oversees three of the City's municipal utilities:

- 1 The Hetch Hetchy project, which consists of water supply and power generating facilities in the Sierra Nevada;
- 2 The water treatment and distribution system, which delivers some of the purest drinking water in the world to more than 2.4 million customers in the Bay Area; and
- 3 The wastewater treatment and disposal system, which collects and treats sewage and storm water flows within San Francisco.

Each of the three utilities represents a separate enterprise within the SFPUC which operates as a department of the City and County of San Francisco. Four divisions are responsible for the operation of the utilities – the Hetch Hetchy Water and Power Division, the Water Supply and Treatment Division, the City Distribution Division, and the Water Pollution Control Division. The SFPUC is governed by a five member Commission appointed for four year terms by the Mayor of San Francisco. The Commission appoints a General Manager who is responsible for day-to-day operations. Final budgetary authority is with the Mayor and the Board of Supervisors.

The SFPUC's utility system originates in the Sierra Nevada, where the Hetch Hetchy Water and Power Division maintains three reservoirs and more than 650 acres of watershed, much of which is located in Yosemite National Park. Water from the reservoirs is conveyed through a series of tunnels and pipelines from the mountains and across the Central Valley. En route, the water passes through four powerhouses, generating 1.5 billion kilowatt hours of hydroelectricity each year for the City's municipal load and customers.

At Tesla Portal in the East Bay, the Hetch Hetchy water becomes the responsibility of the Water Supply and Treatment Division. The Water Supply and Treatment Division also draws another 15% of the total water supply from five reservoirs located in the East Bay and on the Peninsula. Water from these local sources is treated at two plants before it is delivered to City customers and 29 wholesale water surveyors in the San Francisco Bay Area.

At the City of San Francisco's border, the City Distribution Division assumes responsibility for storage and final delivery to San Francisco customers. The Division maintains eleven reservoirs and eight storage tanks within the City, and uses a series of pump stations and more than 1,200 miles of water mains to reach every elevation and corner of the City.

Finally, the City's wastewater discharge and storm water runoff are captured by more than 900 miles of sewers and storm drains. The Water Pollution Control Division maintains the wastewater collection system and operates three treatment plants, where chemical and biological treatment processes are used to remove pollutants before the wastewater is discharged into San Francisco Bay and the Pacific Ocean.

In addition to these four operating divisions, there are eight bureaus that provide technical and administrative support services. This approach eliminates duplication of effort and contributes to more efficient operations.

This annual report highlights the operations and accomplishments of the four divisions and eight bureaus. It also identifies some of the challenges that lie ahead for the SFPUC, including the implementation of a major capital improvement program and expansion into new service areas.

THE COMMISSION

The SFPUC is led by five Commissioners, appointed by the Mayor who serve overlapping four-year terms. The Commission, in turn, elects one of its members to serve as its President each year. The Commission and the Mayor appoint the General Manager who serves as the chief administrative officer and is responsible for the SFPUC's day-to-day operations in accordance with the Commission's policies, the City Charter, and the Administrative Code. The General Manager appoints senior staff to run three utilities.

SAN FRANCISCO PUBLIC UTILITIES COMMISSION MEMBERS DURING FY 1999-2000

E. Dennis Normandy, President
Victor G. Makras, Vice President
Frank L. Cook
Ann Moller Caen
Ashok Kumar Bhatt



E. Dennis Normandy,
President



Victor G. Makras,
Vice President



Frank L. Cook



Ann Moller Caen

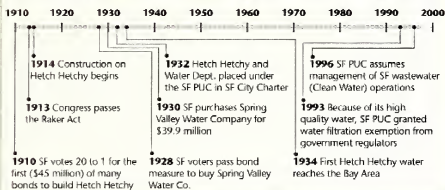


Ashok Kumar Bhatt



San Francisco Public Utilities Commission System Map

Significant SF PUC Historical Dates



Holm Powerhouse



Cherry Power Tunnel

O'Shaughnessy Dam



Hetch Hetchy

Hetch Hetchy Reservoir

Canyon Power Tunnel

Moccasin Reservoir

Priest Reservoir



Moccasin Powerhouse

HETCH HETCHY WATER AND POWER

*H*etch Hetchy Water and Power ("Hetchy") provides water and electricity to retail and wholesale customers. Hetchy currently supplies an average of 220 million gallons per day, or 85% of the drinking water consumed by San Francisco and its 29 Bay Area wholesale customers. Hetchy also supplies 15% of San Francisco's total electric demand.

Hetchy collects and transports water in several reservoirs within federal lands under pre-1914 water rights and rights-of-way granted to the City through federal legislation in 1913 ("the Raker Act"). The purity of Hetchy water makes filtering unnecessary. The Raker Act required Hetchy to develop power generation in order to maximize the beneficial use of the water associated with the project. The Hetchy system today is comprised of 5 reservoirs, 4 hydroelectric power plants and 165 miles of aqueducts and pipelines and 142 miles of power transmission lines which deliver water and power to San Francisco and the Bay Area. In addition, Hetchy has water bank exchange storage in Don Pedro Reservoir and contract rights on PG&E's electric transmission system.

Generation from the Hetchy Project is used first to provide power to City facilities (e.g., City Hall, the Municipal Railway, Moscone Center, the Port, the Airport, Department of Recreation and Parks, City hospitals, City street lighting, water and sewer utilities, etc.). Power is also sold to retail customers in San Francisco and to public agencies and municipalities on a wholesale basis. Hetchy's wholesale customers include the Modesto and Turlock Irrigation Districts which have priority rights under the Raker Act for municipal use and ground water pumping.

As the City's technical expert on power matters, Hetchy represents the City in a wide variety of regulatory, legislative and industry forums on issues related to electric system design, operations and reliability. Hetchy is presently constructing generation, transmission and distribution facilities in San Francisco to facilitate deliveries of electricity to retail customers. Hetchy is also developing a comprehensive program of retail services that will include providing operations and maintenance services and emergency response during power outages. Further, Hetchy is expanding its scope of retail services to include development of the City's full energy efficiency and renewable resource potential.

HIGHLIGHTS FOR 1999-2000

Water Year - Hetch Hetchy Reservoir received about 38 inches of precipitation from 7/1/99 through 6/30/00. During April through July of this year, the snowmelt produced approximately 597,000 acre feet of water, which is about 99% of the historic average and 1.7 times the total capacity of Hetch Hetchy Reservoir. At Lakes Lloyd and Eleanor, the combined April through July inflow was 101% of historic average spring runoff or 318,000 acre-feet of water. Total generation for this period was 1.7 million megawatt hours.

Wildfire - In August, a fire in the watershed necessitated a shut-down of power operations for one week during the summer peak. The cost of purchasing power to meet Hetch Hetchy's firm load commitments during this period was \$630,000.

San Joaquin Pipeline Repairs - Two emergency repairs within 4 months prompted Hetchy to employ state-of-the-art technology to locate and repair weak spots before they became emergencies interrupting water deliveries to PUC customers. To date, more than 30 leaks and weak spots in the pipeline have been identified and repaired.

Y2K - After many months of preparation, Hetchy survived "Y2K" unscathed. Concern for what could go wrong precipitated intense scrutiny of all emergency plans and communications systems to assure that Hetchy could continue to function effectively even in the event of widespread telecommunications and/or power failures.

Watershed Management - Hetch Hetchy employed 350 goats in the Priest watershed to reduce rodent habitat and wildfire potential at a fraction of the cost of conventional means of clearing vegetation. Hetch Hetchy also cleared 7 of the 19 miles of transmission line right of way between Priest and Early Intake of brush and trees to reduce risk of wildfires and to provide access for inspection and maintenance.

Electric Utility Deregulation - Hetch Hetchy continued to represent and protect the City's residents and businesses from adverse impacts of the California electric restructure. In addition, Hetch Hetchy is working diligently with the California Independent System Operator (ISO) and others to strengthen the City's electric system. The PG&E outage of December 8, 1998, coupled with Summer 2000 power resource shortages and emergencies, emphasized the San Francisco Bay Area's extreme vulnerability to power outages.

Filtration Avoidance

The SFPUC along with the five other unfiltered water utilities in the United States successfully negotiated new regulations that will preserve the option to operate the Hetch Hetchy System without filtration. The Federal Advisory Act Committee agreement on future microbial and disinfection by-products regulations requires minimal treatment increases to the existing Hetch Hetchy Aqueduct operational practice. The coordination of strong operations, public outreach, water industry initiatives, and cooperation with other utilities nationally yielded the SFPUC a strong negotiating position to attain these favorable results. These proposed regulations could defer large expenditures of capital for ten or more years.

WATER SUPPLY AND TREATMENT DIVISION

The Water Supply and Treatment Division is responsible for water storage, transmission and treatment; source water protection and environmental stewardship of watersheds; and customer service to both the City Distribution System and suburban wholesale customers. During FY 1999-2000, the Division made progress in the following areas:

Improvement of reliability and functionality of facilities

Major upgrades to facilities typically are designed and managed by the Utilities Engineering Bureau. However, it has been found to be more cost-effective for small engineering and construction jobs to be handled at the Division level. Many of the projects completed this year related to system reliability in terms of both water supply and treatment through provision of back-up power sources and closer monitoring of processes. Examples include the following:

- Improved monitoring and electronic communication in relation to water quality through use of the Supervisory Control Data Acquisition System.
- Overhaul of emergency back-up chemical metering pumps at Tesla Portal, the primary disinfection site for Hetch Hetchy water;
- Construction of an emergency manual disinfection system for Harry Tracy Treatment Plant;

The Division's Maintenance Engineering section has also been active in the design and construction of a number of small construction projects, which included the following:

- Installation of a new chemical feed system at the Sunol Valley Treatment Plant; installation of a pump on the Crystal Springs/San Andreas Pipeline; interlock modifications to Pulgas Pump Station's new by-pass valve; and installation of an air compressor and fuel transfer pump at San Antonio Pump Station;
- Installation of a new filter aid feed system for water treatment at Sunol Valley Treatment Plant; replacement of all filter control systems, allowing automatic backwashing of filters; and installation of a second emergency generator, which provides sufficient back-up power to support the full treatment capacity of the plant.

Watershed Planning and Maintenance

During FY 1999-2000, the City and County of San Francisco's Planning Department took the lead in doing environmental impact analysis of the SFPUC's proposed watershed management plans for its Peninsula and Alameda watersheds. The Land and Resources Section of the Water Supply and Treatment Division provided significant analytical support to this assessment of potential environmental impacts.

The Division has had an ongoing concern in the area of fuel management on the Peninsula Watershed because a catastrophic fire could have such adverse effects on water quality in Peninsula reservoirs, vegetation and wildlife on the Peninsula Watershed, and to property owners adjacent to the watershed. Actions taken to reduce the fuel load on the Peninsula Watershed have included establishing new fuel breaks as well as re-establishing and widening of other fuel breaks.

In response to City legislation related to use of chemicals for pest management, the Division has also been very proactive in implementation of an Integrated Pest Management Program. The Division acquired computer automated spray equipment to accurately apply pesticides where necessary and to reduce the total amount of chemical usage. Water Supply and Treatment also reduced the use of chemical treatments by increased use of hand labor (Conservation Corps) to eradicate the Purple Star Thistle.

Preventive Maintenance of Equipment

During FY 1998-99, the Division's Productivity Task Force completed an analysis that included the recommendation that the Division extend the useful life of its facilities and equipment through implementation of a computerized preventive maintenance program. In water treatment facilities, such maintenance is performed either by craft staff or treatment operators, depending on the nature of the skills and certifications required. During FY 1999-2000, the program was implemented at Harry Tracy Treatment Plant, as a model for future use throughout the Division.

Pipeline Inspection

Operations staff inspected 10 miles of transmission pipelines. Repairs were made as problems were discovered.

Cross Training of Staff

A second recommendation of the Division's Productivity Task Force was to improve the effectiveness and efficiency of staff through cross training. This recommendation was implemented when a mix of staff (including carpenters, plumbers, laborers, electronic maintenance technicians, and apprentice treatment plant operators) received basic training in water treatment processes. One benefit of this training was to prepare plumbers to assume more responsibility for the dechlorination process associated with taking transmission lines in and out of service. Another benefit was to allow craft staff to plan and perform construction and maintenance processes in treatment plants with the benefit of greater understanding of the objectives and mechanics of the treatment process. An additional benefit was the improved teamwork resulting from a greater appreciation on the part of craft staff of the challenges associated with the treatment process.

Y2K Preparedness

Water Supply and Treatment Division developed a comprehensive emergency preparedness plan to deal with the Y2K rollover. This included an extensive review of Division equipment and mitigation as required.



The SFPUC watershed keepers are responsible stewards of the land as well as vigilant protectors of our drinking water.



CITY DISTRIBUTION DIVISION

The City Distribution Division stores, distributes, treats, and delivers water directly to customers in San Francisco. The Division maintains the water distribution system within the City, which consists of reservoirs and auxiliary tanks, pumping stations and a network of approximately 1,250 miles of pipelines. On average, the Division delivers approximately 80 million gallons of water a day to nearly 770,000 people within the City.

The City Distribution Division (CDD) conducts a range of services including providing 24 hour-a-day response capability for water main breaks and for pumping, pressurizing and disinfection of the water distribution system. CDD also provides information on the in-City water distribution system to utilities, developers, owners and the general public. During all multiple alarm fires in the City, CDD responds to assure there is sufficient water pressure and supply to suppress the fire.



Reservoirs and pumping stations in San Francisco. The water system in San Francisco consists of over 1,200 miles of pipe, the distance between San Francisco and Denver.

In addition, the City Distribution Division:

- Operates and maintains 18 pumping stations supplying 10 reservoirs, and 7 storage tanks.
- Maintains, repairs and upgrades as necessary 1,250 miles of water mains and over 15,000 gate valves.
- Protects and coordinates work done by others to assure that San Francisco Water Department facilities are not damaged or destroyed.
- Installs, repairs and maintains services connecting individual customers to water mains.
- Identifies and repairs underground leaks.
- Performs landscape maintenance of 984 acres of Division land, including right-of-ways, reservoirs, open space and parks.

HIGHLIGHTS FROM 1999 - 2000

Water Main Repair and Replacement - The division made the following types of repairs:

| | |
|---------------------------------|-----|
| Cast Iron Main breaks | 73 |
| Connections | 103 |
| Main extensions and relocations | 3 |
| Steel main leaks | 4 |
| Cut in new gate services | 36 |

Service Renewals - Water services connect individual customers with the City's water mains.

| | |
|---------------------|------|
| New services | 764 |
| Service renewals | 962 |
| Meter installations | 6287 |
| Service Maintenance | 6529 |

Meter Replacement -The Division has an ongoing program to monitor and replace the more than 167,000 meters that measure the amount of water delivered to each customer. This year 6,563 meters were replaced.

Treasure Island - Treasure Island/Yerba Buena is served from the San Francisco Water Department (SFWD) City Distribution system through a pump station at the base of the Bay Bridge. CDD crews operate and maintain the island's water system under a limited set of guidelines. Efforts from Cal Trans to seismically upgrade the Bay Bridge mandated the current pump station to be relocated. The City worked with Cal Trans to determine a site and design a new pump station. In August 1999, Construction began to replace the old Bay Bridge Pump Station to be located at the corner of Bryant and Main Streets. The new Pump Station, equipped with back-up pumps, emergency power and SCADA compatibility, was completed in June 2000.

Replacement of Ballast Twin Pipes

The Two University Mound feeder mains cross under a bridge of the Interstate 280 Freeway, just west of the Alemany Interchange. The pipes were supported on concrete saddles, but had no anchorage against movement potentially caused by a large earthquake. These pipelines are critical to maintaining service to downtown San Francisco and were particularly vulnerable until replacement. In November 1999, construction for the replacement of the twin pipelines began. Both pipes were then anchored to the saddles, and covered with sand to ballast them against movement during an earthquake. This project deals with system reliability, maintenance and improvement of the infrastructure and facilities.

LOOKING FORWARD

The Division, working with the Utilities Engineering Bureau and Water Quality Bureau, intends to continue much needed repairs to reservoirs, pump stations, storage tanks and other facilities that are reaching or have exceeded their life expectancy.



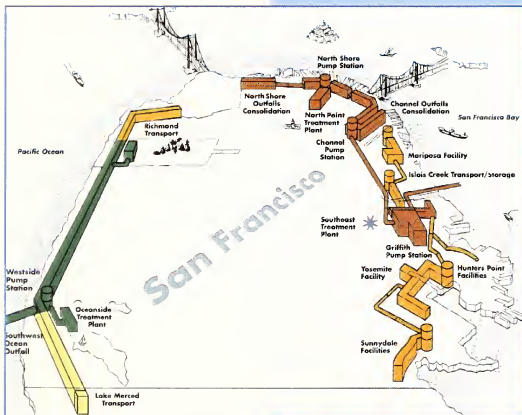
The SFPUC oversees the maintenance of 1,200 miles of water mains and more than 900 miles of sewers and storm drains.

WATER POLLUTION CONTROL DIVISION

W

ater Pollution Control is charged with the collection, treatment, and discharge of sanitary and stormwater flows generated within the City and County of San Francisco and manages the Southeast Community Facility. The Division is organized into seven sections: Operations, Maintenance, Sewer Operations, Administration, Southeast Community Facility, Engineering, and Safety. Since the construction of the Clean Water Enterprise facilities in the 70's and 80's, this team has provided the operation and maintenance of those facilities and achieved a superior level of performance protecting public health and insuring environmental safety of the waters surrounding San Francisco.

As with most companies world wide, Water Pollution Control faced the serious threat that computers and the equipment they control might not function on January 1, 2000 because of the "Y2K bug". Planning was initiated eighteen months prior to the Y2K date. Through an exhaustive field inspection program, faulty and suspect systems were identified; equipment was repaired, replaced, or mitigated; documentation was maintained to verify actions taken; operational scenarios were tested to react to unforeseen emergencies; and a "pre-event" audit was completed. Water Pollution Control also participated in the City wide Y2K effort that predicted unusually large crowds would be on the streets celebrating the New Year. Because of extensive planning, there were no Y2K problems. Water Pollution Control is now taking further advantage of the Y2K planning and documentation by converting it into emergency preparedness plans.



A schematic map of the wastewater system.

OPERATION HIGHLIGHTS FROM 1999-2000

- Operations division combined the Oceanside and Bayside functions under one management structure. The new organization is more efficient and also provides a more effective response to staff shortages and emergencies.
- The Oceanside Operations Division received the Association of Metropolitan Sewerage Agencies' Gold Award for excellent compliance with discharge permit conditions for calendar year 1999.
- The Oceanside Treatment Plant processed 7.5 billion gallons of sanitary and storm runoff this past year. Storm water facilities captured and discharged 1.1 billion gallons through the Southwest Ocean Outfall allowing only seven "near shore" discharges; the system is designed for eight per year.
- The Southeast Treatment Plant processed 28.1 billion gallons of sanitary and storm runoff this past year. There were three collection system discharges in the North Basin, twelve discharges in the Central Basin and one discharge in the South Basin. The North, Central and South Basins are designed for a total of seventeen discharges per year: four for the North, twelve for the Central and one for the South Basin area.
- The North Point Treatment Plant, used only during heavy rainfall, processed 1.2 billion gallons of sanitary and storm runoff.

Water Pollution Control has implemented a renewed commitment to the Sewer Operations management team and infrastructure. Sewer Operations is directly responsible for customer response, sewer inspections and cleaning. Structural problems are referred to the Department of Public Works and the SFPUC Utilities Engineering Bureau. Sewer Operations responded to 8,323 calls, performed 1,985 inspections, and requested repair at 538 locations.

CONSERVATION HIGHLIGHTS 1999 - 2000

Water Pollution Control remains active in conservation efforts.

- This Division was the first in the City to purchase an electric passenger vehicle and now has a second electric vehicle.
- In cooperation with the California Independent System Operator, Water Pollution Control has curtailed electrical use during peak periods by shutting down treatment operations. Sanitary sewage is stored in the transport/storage boxes for treatment later in the day when electrical loads are reduced.
- It has been standard practice at treatment facilities in San Francisco to recycle everything possible especially by reducing the need for fresh water where treated effluent can be employed. Biosolids are now used at landfill sites as daily cover to help contain other materials.
- Water Pollution Control received an award for being in the "top ten" of the City's recycling effort with a special award to the Southeast Community Facility.

SFPUC BUREAUS

The four operating divisions receive technical and administrative support from eight service bureaus. This approach eliminates duplication of efforts and contributes to more efficient operations. Several functions have been reassigned among the bureaus to improve services to the operating divisions and, ultimately, to customers.

UTILITIES ENGINEERING BUREAU

The Utilities Engineering Bureau (UEB) provides project management, engineering, construction management, and contracting services for the water, power and wastewater capital improvement programs of the San Francisco Public Utilities Commission (SFPUC). UEB manages the construction of facilities and implements necessary upgrades and repairs. In 1999-2000, UEB was responsible for almost \$206 million in capital improvement contracts to water, wastewater and power facilities, and the award of 54 construction contracts, including emergencies, for over \$77 million.

HIGHLIGHTS FROM 1999-2000

- Managed the process resulting in the selection of the San Francisco Water Alliance as consultant for a contract, not to exceed \$45 million and with a duration of 4 years, to provide for program management services for the SFPUC's large Capital Improvement Program.
- Completed detail design on the Sunol Valley Water Treatment Plant Interim Improvements, Phase No. 1, to provide \$46 million in improvements to meet water quality regulations and ensure the reliability of the plant.
- Began construction on the phased Supervisory Control Data Acquisition (SCADA) project to install a system-wide monitoring and control system for the City's water system. The SCADA system will provide coverage of the SFPUC's water transmission and distribution system from the impounding reservoirs in the Sierras, East Bay and Peninsula, all the way to the City. The work under this project is geographically dispersed and will ultimately affect three hundred sites.

INFORMATION TECHNOLOGY SYSTEMS

The Information Technology Systems Bureau (ITS) provides data processing, computer systems development and office automation services to all SFPUC divisions and bureaus. The Bureau maintains and improves computer systems for processing water and sewer billing data, facilities maintenance data, payroll and other financial data. To support these and other functions, the Bureau also maintains a computer network of more than 1000 microcomputers, which are installed throughout various SFPUC locations.

HIGHLIGHTS FROM 1999-2000

In 1999-2000 the Bureau made the following improvements in the SFPUC computerized systems:

- Replaced hard copy financial and personnel vacancy reports with more timely and efficient Intranet access to this data.
- Implemented new customer payment options including automatic payment of bills directly from customer's checking accounts and credit card payments by phone, using an interactive voice response system.
- Installed 300 networked computers for increased personal efficiency and improved data sharing among the various organizational units.

PERSONNEL AND TRAINING

The Bureau of Personnel and Training provides services related to human resource and payroll management and acts as the liaison with the Department of Human Resources, the Civil Service Commission, and the Controller's Payroll Services Division. Bureau functions include: classification, examination, payroll position control, labor relations, disciplinary matters, equal opportunity compliance, training, and general personnel administration. The 1999-2000 year presented ongoing challenges to the Bureau in its efforts to keep up with the growth of the SFPUC.



HIGHLIGHTS FROM 1999 2000

- Concluded training to all employees in "Prevention of Sexual Harassment and Gender at Work." Concluded training to all supervisors in conducting investigations and offered training in performance appraisals. Conducted training for Departmental Personnel Liaisons in the Family Medical Leave Act.
- Successfully transitioned the requisition process from a Department of Human Resources-centralized process to a SFPUC-based decentralized model.
- Permanent appointments were made in the Program Manager series, which cut down on the overall number of Special Assistants according to a directive from the Civil Service Commission.
- Administered 18 examinations.
- Filled 441 permanent and temporary positions, reducing the vacancy rate to 8%.
- Published a supervisory handbook on the intranet.
- Coordinated 62 Registry selections.
- Administered 65 Provisional Exams.

WATER QUALITY

The mission of the Water Quality Bureau (WQB) is: to ensure that the PUC complies with all current and future water quality regulations through sampling and analysis, process engineering, applied research, inspections, field project oversight, regulatory reporting and development, and direct operations support; to analyze discharges (into the sewer system, Bay, and Ocean), assess environmental effects, and recommend any necessary mitigation; to respond to consumer complaints/inquiries about drinking and receiving water quality; and to promote the health, safety, professional development, and diversity of its staff.

The WQB accomplishes this mission throughout the PUC "snowfall to outfall" service area — from Yosemite National Park to the Pacific Ocean.

The WQB is comprised of four sections: Administration, Engineering, Environmental Services, and Laboratories.

HIGHLIGHTS FROM 1999-2000

Laboratory Section:

- Performed more than 13,000 analytical tests (organic, inorganic, metals, and biological) on source and treated waters from reservoirs, pipelines, and distribution systems to assure compliance with water quality regulations for the drinking water supply.
- Conducted over 22,000 analytical tests on pretreatment samples, wastewater discharges and to assure compliance with discharge permits.
- Initiated four new analytical methods that were formerly contracted to commercial laboratories.



Environmental Services:

- Processed 7200 backflow prevention device tests and inspected 431 new water installations to prevent contamination of drinking water with unsanitary sources. Completed Tracer study to evaluate if the San Francisco Fire Department's high pressure Auxiliary Water Supply System fire fighting water line was cross-connected with the potable drinking water distribution system. 24,000 separate services were inspected with a single cross-connection found.
- Completed the Environmental Protection Agency's (EPA) mandated Information Collection Rule (ICR) project, a national data gathering effort for the preparation of future regulations.
- Completed a two year program to provide free lead in tap water testing for citizens of San Francisco who qualified through the Women, Infants, and Children (WIC) program. Initiated a voucher program to continue free lead testing for San Francisco residents.
- Responded in the field to more than 239 consumer complaints within four hours of initial contact.

Engineering Section

- Investigated and monitored the quality of five turbidity spikes in the San Joaquin pipeline due to flow rate changes.



Educating young people about water quality issues and wastewater treatment is a priority for the SFPUC. Over 500 tours are conducted each year at wastewater facilities and treatment plants.

- Performed watershed field investigations of potential contaminant sources in the Hetch Hetchy, Lake Eleanor, Cherry Lake, Early Intake, and Priest and Moccasin watersheds.
- Prepared, and submitted to the Department of Health Services Annual Sanitary Survey Update Report for the Hetch Hetchy Supply.
- Reviewed six proposed drinking water regulations and provided comments and suggestion to the regulatory agencies.
- Completed Computational Fluid Dynamic Modeling of various City reservoirs to assess their existing conditions and provide recommendations for improving their hydraulics in preparation for the upcoming chloramine conversion.
- Completed the City Distribution System Monitoring Plan for the upcoming conversion to chloramine.

CUSTOMER SERVICE

The Customer Service Bureau is the primary point of contact with the SFPUC for water and sewer customers. The Bureau maintains 145,837 residential accounts and 21,528 commercial and municipal accounts in San Francisco. The Bureau provides billing and collection of water and sewer charges, administration of customer accounts (including opening and closing accounts), installation of new services, meter reading, and field services such as inspections. The Bureau oversees the ultra-low flow toilet rebate and give-away programs and administers the "best management practices", a water conservation program.

The Customer Service Bureau is also responsible for the development of public information programs for water and sewer construction projects, and serves as an administrative source for water and sewer complaints.

HIGHLIGHTS FROM 1999-2000

- Customer Accounts Section established centralized Customer Assistance Unit (CAU) which was successful in offering various alternative payment options to customers. After one year of offering Automatic Bill Payment service, the goal of 15,000 enrollments or 10% of residential customers was met. The Chinatown Payment Station began accepting payments for water and sewer services and over 4,000 payments have been made there in the 1st year.

- The Customer Assistance Unit (CAU) staff all received cross training on how to calculate water and sewer charges, auditing bills on the exception register, payment processing and the delinquency process. While training was taking place, the daily operations were still completed without delays. On February 2, 2000, the CAU went "live".
- Within the first six months of initiation, the CAU answered 30,800 customer calls or an average of 220 calls each day. Since February, the CAU has responded to 15,000 calls or an average of 150 calls per day. The number of calls decreased because the need to transfer calls within the Section declined because the CAU is responding to 95% of all billing, payment and collection questions.
- The Auditing Unit, reviewed 103,000 customer accounts and issued over 19,000 field inspection work orders and assisted 12,520 customers by phone.
- The Collection & Lien Unit, reported just under 5,000 lien recorded totaling \$2.2 million. Over 5,000 48 - Hour Notices were issued and of those 26% of the accounts, or 1,389, were actually shut off. The delinquency process without liens, collected over \$2 million in revenue.

COMMERCIAL LAND MANAGEMENT

The Bureau of Commercial Land Management manages the SFPUC's commercial interest in lands and properties owned by the SFPUC. The Bureau monitors lease and permit negotiations, insurance renewals, delinquent rent collections, property taxes and assessments, and land sales and purchases.

Its staff also recommends policies to the SFPUC and implements procedures approved by the SFPUC relating to land use, rental, management, and disposal of properties under its control. The Bureau seeks to identify means of increasing revenues by developing innovative uses of pipeline rights-of-way, treatment facilities, and watershed properties in a manner consistent with the goals of the SFPUC.

HIGHLIGHTS FROM 1999-2000

- Increased annual rent revenues by approximately 1 million dollars.
- Negotiated approximately 30 new leases and permits.

BUREAU OF SYSTEM PLANNING, ENVIRONMENT AND COMPLIANCE

The Bureau of System Planning, Environment and Compliance is responsible for:



- Planning for the continued service of reliable high quality water to San Francisco and its customers, and the continued collection, treatment and disposal of wastewater for San Francisco in compliance with current and anticipate laws and regulations.
- Protecting the environment, our citizens, employees and facilities by regulating industrial waste discharges to the sewerage system and implementing the sewer user charge program.
- Assisting the PUC in complying with and implementing environmental and regulatory compliance efforts.

The Bureau is a merger of the Bureau of Environmental Regulation and Management and System Planning and Regulatory Compliance.

HIGHLIGHTS FROM 1999-2000

- In 1998-99, the System Planning Bureau undertook the preparation of Capital program priorities for each of the SFPUC enterprises – Water, Clean Water and Hetch Hetchy. The purpose of these reports was to prioritize the Capital Improvement needs of each operating division, based on input from staff and managers of the operating divisions, Utilities Engineering Bureau and Water Quality Bureau. An implementation plan and schedule of funding required to support the overall SFPUC capital program is currently being prepared.
- Received the Public Education Award from the Association of Metropolitan Sewage Agencies (AMSA) for developing and implementing the less toxic pest control program.
- Identified and verified all commercial stormwater sources in the City.
- Successfully assisted all PUC facilities in complying with the underground storage tank regulations and requirements.
- Completed conceptual engineering for the conversion of the Hetch Hetchy water treatment to chloramine.
- Sunol Filter Plant conceptual engineering for near term improvements were nearly completed and capacity upgrades concept was approved by the SFPUC.



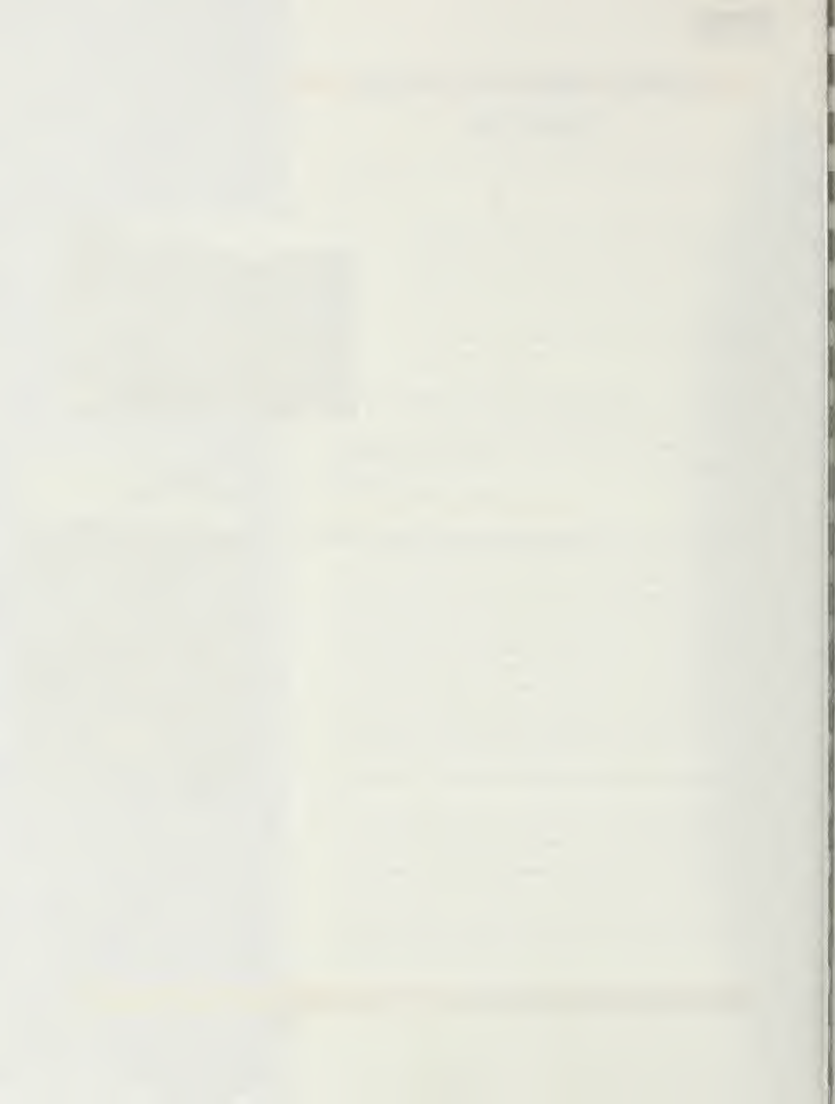
The scenic Sawyer Camp Trail and the Crystal Springs Trail are open to the public to partake of the vistas every day of the week from 8 AM to 5 PM.

SAN FRANCISCO CLEAN WATER PROGRAM

Financial Statements

June 30, 2000 and 1999

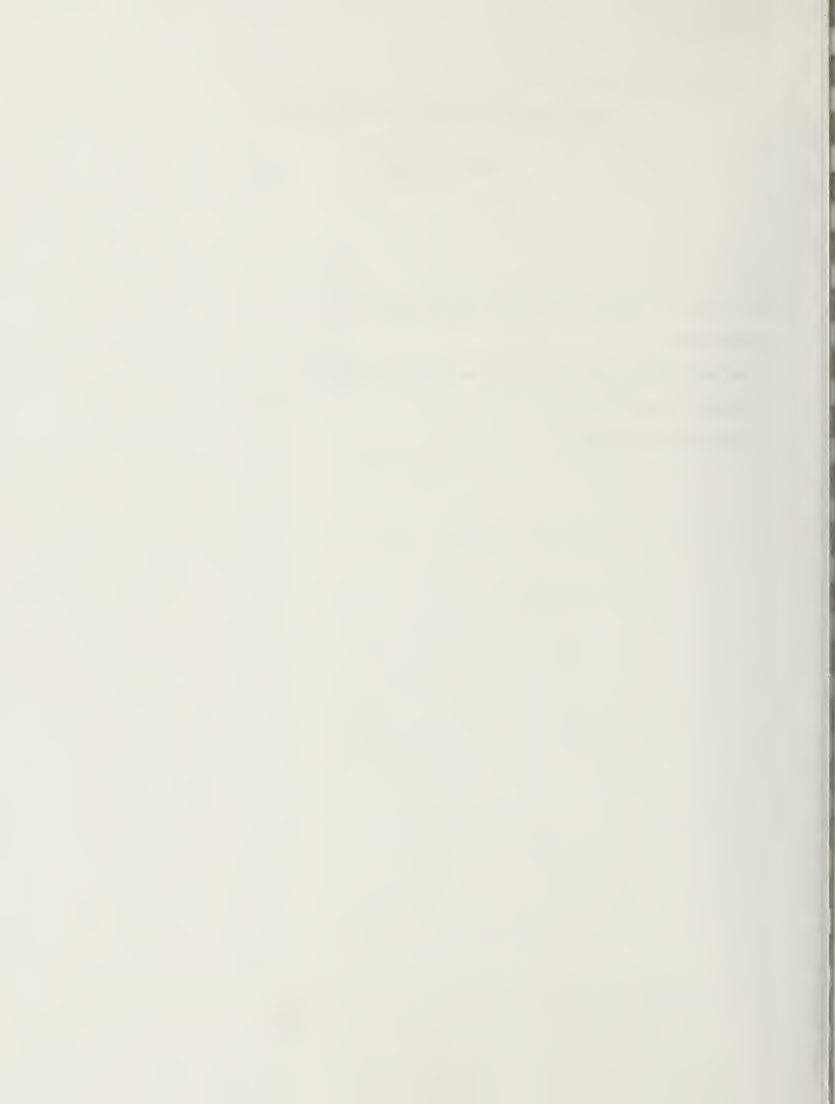
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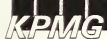


SAN FRANCISCO CLEAN WATER PROGRAM

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Three Embarcadero Center
San Francisco, CA 94111

Independent Auditors' Report

Honorable Mayor and Board of Supervisors
City and County of San Francisco, California:

We have audited the accompanying financial statements of the San Francisco Clean Water Program (the Program) of the City and County of San Francisco, California (the City), as of and for the years ended June 30, 2000 and 1999, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 1, the financial statements referred to above present only the financial activities of the Program and are not intended to present fairly the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Francisco Clean Water Program of the City and County of San Francisco, California, as of June 30, 2000 and 1999, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

October 25, 2000



KPMG LLP, KPMG LLP, a U.S. limited liability partnership, is
a member of KPMG International, a Swiss association

SAN FRANCISCO CLEAN WATER PROGRAM

Balance Sheets

June 30, 2000 and 1999
(in thousands)

| Assets | 2000 | 1999 |
|---|--------------|-----------|
| Current assets: | | |
| Deposits and investments with City Treasury | \$ 58,300 | 49,006 |
| Receivables: | | |
| Charges for services (net of allowance for doubtful accounts of \$1,000 and \$1,500 in 2000 and 1999, respectively) | 28,647 | 27,899 |
| Interest and other | 754 | — |
| Total receivables | 29,401 | 27,899 |
| Total current assets | 87,701 | 76,905 |
| Restricted assets: | | |
| Deposits and investments with City Treasury | 122,739 | 110,884 |
| Deposits and investments outside City Treasury | 41,270 | 39,570 |
| Interest receivable | 1,173 | 2,022 |
| Total restricted assets | 165,182 | 152,476 |
| Fixed assets, net | 1,379,755 | 1,394,830 |
| Bond issuance costs, net of accumulated amortization of \$1,213 in 2000 and \$1,031 in 1999 | 3,011 | 3,193 |
| Total assets | \$ 1,635,649 | 1,627,404 |
| Liabilities and Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 1,812 | 1,285 |
| Accrued payroll | 1,805 | 2,117 |
| Accrued vacation and sick leave, current portion | 1,725 | 1,039 |
| Accrued workers' compensation, current portion | 406 | 323 |
| Damage and claims liability, current portion | 104 | 335 |
| Bond interest payable | 9,292 | 9,707 |
| Revenue bonds, current portion | 22,275 | 20,710 |
| State revolving fund loans, current portion | 12,998 | 11,135 |
| Total current liabilities | 50,417 | 46,651 |
| Liabilities payable from restricted assets | 3,791 | 4,926 |
| Deferred revenue and other long-term liabilities: | | |
| Accrued vacation and sick leave | 1,490 | 860 |
| Accrued workers' compensation | 1,153 | 810 |
| Damage and claims liability | 329 | 975 |
| Deferred revenue | 3,329 | 4,308 |
| Total deferred revenue and other long-term liabilities | 6,301 | 6,953 |
| Long-term debt, less current portion: | | |
| Revenue bonds | 453,447 | 474,063 |
| State revolving fund loans | 167,297 | 156,595 |
| Total long-term debt | 620,744 | 630,658 |
| Total liabilities | 681,253 | 689,188 |
| Equity: | | |
| Contributed capital | 595,203 | 607,964 |
| Retained earnings – reserved for bond requirements and other commitments | 29,360 | 26,959 |
| Retained earnings – unreserved | 329,833 | 303,293 |
| Total retained earnings | 359,193 | 330,252 |
| Total equity | 954,396 | 938,216 |
| Total liabilities and equity | \$ 1,635,649 | 1,627,404 |

See accompanying notes to financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM

Statements of Revenues, Expenses, and Changes in Retained Earnings

Years ended June 30, 2000 and 1999

(in thousands)

| | <u>2000</u> | <u>1999</u> |
|---|-------------------|-----------------|
| Operating revenues: | | |
| Charges for services | \$ 140,878 | 138,872 |
| Other revenues | 4,617 | 4,102 |
| Total operating revenues | <u>145,495</u> | <u>142,974</u> |
| Operating expenses: | | |
| Personal services | 30,020 | 26,248 |
| Contractual services | 5,843 | 6,336 |
| Materials and supplies | 6,013 | 5,588 |
| Depreciation | 38,169 | 37,538 |
| Bad debts | — | 380 |
| Services provided by other departments | 16,142 | 18,953 |
| General and administrative | 9,903 | 9,808 |
| Other | 9,183 | 4,672 |
| Total operating expenses | <u>115,273</u> | <u>109,523</u> |
| Operating income | <u>30,222</u> | <u>33,451</u> |
| Nonoperating revenues (expenses): | | |
| Federal | 222 | 822 |
| State/other | 130 | 15 |
| Interest and investment income | 8,674 | 9,749 |
| Interest expense | (31,902) | (33,596) |
| Other, net | 8,834 | (255) |
| Net nonoperating expenses | <u>(14,042)</u> | <u>(23,265)</u> |
| Income before operating transfers | <u>16,180</u> | <u>10,186</u> |
| Operating transfers from the City and County of San Francisco | <u>—</u> | <u>4,753</u> |
| Net income | <u>16,180</u> | <u>14,939</u> |
| Depreciation expenses against contributed capital | 12,761 | 14,425 |
| Retained earnings at beginning of year | <u>330,252</u> | <u>300,888</u> |
| Retained earnings at end of year | <u>\$ 359,193</u> | <u>330,252</u> |

See accompanying notes to financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM

Statements of Cash Flows

Years ended June 30, 2000 and 1999

(in thousands)

| | 2000 | 1999 |
|---|------------|----------|
| Cash flows from operating activities: | | |
| Cash received from customers, including cash deposits | \$ 144,747 | 142,201 |
| Cash paid to employees for services | (29,016) | (25,876) |
| Cash paid to suppliers for goods and services | (20,512) | (14,738) |
| Cash paid for quasi-external transactions | (25,300) | (29,047) |
| Cash paid for judgments and claims | (1,196) | (6,119) |
| Net cash provided by operating activities | 68,723 | 66,421 |
| Cash flows provided by noncapital financing activities – operating grants | 352 | 837 |
| Cash flows from financing activities: | | |
| Capital grants | — | 1,706 |
| State revolving fund loan proceeds | 23,700 | — |
| Transfers from the City for debt service | — | 4,753 |
| Acquisition and construction of capital assets | (22,957) | (34,189) |
| Interest paid on long-term debt | (32,395) | (34,965) |
| Principal paid on long-term debt | (20,710) | (22,990) |
| Principal paid on loans | (11,135) | (10,874) |
| Net cash used in financing activities | (63,497) | (96,559) |
| Cash flows from investing activities: | | |
| Interest income received | 8,830 | 10,472 |
| Proceeds from sale of investments | 44,381 | 43,841 |
| Purchase of investments | (45,993) | (44,979) |
| Purchase of restricted deposits and investments | (3,890) | (3,933) |
| Proceeds from sale of restricted deposits and investments | 3,890 | 7,802 |
| Proceeds from insurance claims | 8,176 | — |
| Other investing activities | 1,318 | 405 |
| Net cash provided by investing activities | 16,712 | 13,608 |
| Increase (decrease) in cash and cash equivalents | 22,290 | (15,693) |
| Cash and cash equivalents: | | |
| Beginning of year | 161,332 | 177,025 |
| End of year | \$ 183,622 | 161,332 |

SAN FRANCISCO CLEAN WATER PROGRAM

Statements of Cash Flows

Years ended June 30, 2000 and 1999

(in thousands)

| | <u>2000</u> | <u>1999</u> |
|--|-------------------|----------------|
| Reconciliation of operating income to net cash provided by operating activities: | | |
| Operating income | \$ 30,222 | 33,451 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | |
| Depreciation | 38,169 | 37,538 |
| (Recovery of) provision for uncollectible accounts | (500) | 380 |
| Changes in assets and liabilities: | | |
| Receivables – charges for services, net | (248) | (773) |
| Payables: | | |
| Accounts payable | 527 | (64) |
| Accrued payroll | (312) | 214 |
| Accrued vacation and sick leave | 1,316 | 158 |
| Accrued workers' compensation | 426 | 625 |
| Damage and claims liability | (877) | (5,108) |
| Net cash provided by operating activities | <u>\$ 68,723</u> | <u>66,421</u> |
| Reconciliation of cash and cash equivalents to the balance sheet: | | |
| Deposits and investments with City Treasury: | | |
| Unrestricted | \$ 58,300 | 49,006 |
| Restricted | <u>122,739</u> | <u>110,884</u> |
| Total deposits and investments | 181,039 | 159,890 |
| Add restricted deposits outside City Treasury meeting the definition of cash equivalents | <u>2,583</u> | <u>1,442</u> |
| Cash and cash equivalents at end of year on statement of cash flows | <u>\$ 183,622</u> | <u>161,332</u> |
| Noncash investing, capital and financing activities: | | |
| Depreciation on contributed capital | <u>\$ 12,761</u> | <u>14,425</u> |

See accompanying notes to financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(1) The Financial Reporting Entity

The San Francisco Clean Water Program (the Program) was established in 1977 following the transfer of all sewage-system-related assets and liabilities of the City and County of San Francisco (the City) to the Program on July 1, 1977, which was the first day of the fiscal year in which the San Francisco Series A Sewer Revenue Bonds of 1976 were issued.

In 1976, the electorate of the City approved a proposition authorizing the City to issue \$240,000 in revenue bonds pursuant to the Revenue Bond Law of 1941 of the State of California for the purpose of acquiring, constructing, improving, and financing improvements to the City's municipal sewage treatment and disposal system. Since then, the City's Board of Supervisors has adopted resolutions (the Clean Water Resolutions) providing for the issuance of various sewer revenue and refunding bond series. As of June 30, 1993, the City had exhausted its bonding capacity under the 1976 proposition approved by the electorate. The Clean Water Resolutions require the City to keep separate books of records and accounts of the Program.

The San Francisco Public Utilities Commission (the Commission), established in 1932, is responsible for providing operational oversight of the public utility enterprises of the City, which include the Program along with the City's power and water utilities (e.g., Hetch Hetchy Water and Power [Hetch Hetchy] and the San Francisco Water Department [SFWD]). The Commission consists of five members appointed by the Mayor who are responsible for determining such matters as the rates and charges for services, approval of contracts, and organizational policy. The Commission is a department of the City and, as such, the financial operations of the Program, Hetch Hetchy, and the SFWD are included in the Comprehensive Annual Financial Report of the City as enterprise funds. These financial statements present only the financial operations of the Program and are not intended to present the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types.

(2) Significant Accounting Policies

(a) *Basis of Accounting—Fund Accounting*

The accounts of the Program are organized on the basis of a proprietary fund type, specifically an enterprise fund. The operations of this fund are accounted for with a separate set of self-balancing accounts that comprise the Program's assets, liabilities, fund equity, revenues, and expenses. Enterprise Funds account for operations (i) that are financed and operated in a manner similar to private business enterprises where the intent of the Commission is that the Program's costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or (ii) where the Commission has decided that periodic determination of revenues earned, expenses incurred, and net income or loss of the Program is appropriate for capital maintenance, public policy, management control, accountability, or other purpose.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

(b) *Measurement Focus*

The financial activities of the Program are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Under this method, all assets and liabilities associated with operations are included on the balance sheet; revenues are recorded when earned and expenses are recorded when liabilities are incurred.

The Program does not apply Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989. The Program applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as statements and interpretations of FASB, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

(c) *Cash and Cash Equivalents*

Cash and cash equivalents include all highly liquid investments, including restricted assets, with an original purchased maturity of three months or less.

(d) *Investments*

Certain investments are stated at fair value based upon quoted market prices. Changes in fair value are recognized as investment income.

Money market funds that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost.

(e) *Fixed Assets*

Fixed assets with an original acquisition date prior to July 1, 1977 are recorded in the financial statements at estimated cost, as determined by an independent professional appraisal, or at cost, if known. All subsequent acquisitions have been recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets which range from 3 to 75 years. No depreciation or amortization is recorded in the year of acquisition and a full year's depreciation or amortization is recorded in the year of disposal.

(f) *Construction in Progress*

The cost of acquisition and construction of major plant and equipment is recorded as construction in progress. As facilities are accepted by the Program and become operative, they are transferred to the plant and equipment accounts and depreciated in accordance with the Program's depreciation policies. Costs of construction projects that are discontinued are recorded as expense in the year in which the decision is made to discontinue such projects.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(g) Capitalization of Interest

A portion of the interest cost incurred on capital projects is capitalized on assets that require a period of time for construction or to otherwise prepare them for their intended use. Such amounts are amortized over the useful lives of the assets.

(h) Bond Discount and Issuance Costs

Bond discount and issuance costs are amortized over the term of the related bonds.

(i) Accrued Vacation and Sick Leave

Accrued vacation pay, which may be accumulated up to ten weeks per employee, is charged to expense as earned. Unused sick leave accumulated through December 6, 1978 is vested and payable upon termination of employment by retirement, death, or disability caused by industrial accident. Sick leave earned subsequent to that date is nonvesting and may be accumulated up to six months per employee.

(j) Workers' Compensation

The Program is self-insured for workers' compensation claims and accrues the estimated cost of those claims, including the estimated cost of incurred but not reported claims.

(k) Damage and Claims Liability

The Program is self-insured for general liability and property damage claims. The liability represents an estimate of the cost of all outstanding claims, including adverse loss development, and estimated incurred but not reported claims.

(l) Arbitrage Rebate Payable

Certain bonds are subject to arbitrage rebate requirements in accordance with regulations issued by the U.S. Treasury Department. The requirements generally stipulate that earnings from the investment of the tax-exempt bond proceeds that exceed related interest costs on the bonds must be remitted to the federal government on every fifth anniversary of each bond issue. There was no arbitrage rebate liability as of June 30, 2000 and 1999.

(m) Refunding of Debt

Gains or losses occurring from advance refundings of debt are deferred and amortized into interest expense over the remaining life of the old bonds or the life of the new bonds, whichever is shorter.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

(n) *Income Taxes*

As a government agency, the Program is exempt from both federal income taxes and California state franchise taxes.

(o) *Contribution from the City and County of San Francisco*

The net book value of all assets and liabilities, including liabilities under sewage-related general obligation bonds relating to the sewage system transferred from the City to the Program, are reflected as contributed capital in the accompanying financial statements.

(p) *Revenue Recognition*

Sewer service charges are based on water usage as determined by the SFWD. Billings are on a monthly or bimonthly basis. Revenues reflected in the financial statements include accruals based on estimates for the periods between termination of the billing cycle and the end of the fiscal year.

Sewer revenue rates must be set to produce sufficient revenue to fund the obligations of the Program as defined in the Clean Water Resolutions, including costs for operation, maintenance, repair and replacements, revenue bond debt service and compliance with federal and state laws and regulations. In addition, City Ordinance No. 198-77 requires that rates be recommended annually to produce sufficient revenue (except to the extent that funds are provided by transfers from other City funds – note 11) to pay debt service on sewage-related general obligation bonds (note 7).

In June 1998, the voters passed Proposition H, which effectively froze the sewer rates at the levels in effect as of January 1, 1998 until July 1, 2006, subject to certain exceptions such as to service pre-existing debt. The passage of Proposition H limits the Program's ability to fund future sewer maintenance projects and/or meet new federal or state regulations that may arise during the period in which Proposition H is effective.

(q) *Contributed Capital*

The Program receives federal and state grants for the purpose of acquisition or construction of property and equipment. These grants are recorded as contributed capital when the grant is earned. Grants are generally earned upon expenditure of funds. The gross amount of depreciation is presented as an expense in the statement of revenues, expenses, and changes in retained earnings with the portion of depreciation relating to assets acquired with capital grants being added back after net income and closed to contributed capital.

(r) *Use of Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(s) *Reclassifications*

Certain reclassifications have been made to the 1999 financial statements to conform to the 2000 presentation. These reclassifications did not change total assets, liabilities, equity or net income.

(3) **Reserved Retained Earnings**

Calculation of reserved retained earnings as of June 30, 2000:

| | | |
|---|----|----------------|
| Restricted assets | | |
| Deposits and investments with City Treasury | \$ | 122,739 |
| Deposits and investments outside City Treasury | | 41,270 |
| Grants and other receivables | | <u>1,173</u> |
| Total restricted assets | | 165,182 |
| Less: | | |
| Bond construction funds | | 122,739 |
| Accrued interest payable on bond proceeds | | 9,292 |
| Liabilities payable from restricted assets | | <u>3,791</u> |
| Reserved retained earnings | \$ | <u>29,360</u> |
| Total retained earnings | \$ | 359,193 |
| Less reserved retained earnings as calculated above | | <u>29,360</u> |
| Unreserved retained earnings | \$ | <u>329,833</u> |

(4) **Cash and Investments**

The captions on the balance sheet related to cash and investments as of June 30, 2000 and 1999 are as follows:

| | <u>2000</u> | <u>1999</u> |
|--|-------------------|----------------|
| Deposits and investments with City Treasury: | | |
| Unrestricted – pooled | \$ 58,300 | 49,006 |
| Restricted – pooled and nonpooled (note 6) | 122,739 | 110,884 |
| Deposits and investments outside City Treasury – restricted (note 6) | <u>41,270</u> | <u>39,570</u> |
| | <u>\$ 222,309</u> | <u>199,460</u> |

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

Investments

The Program's deposits and investments with the City Treasury are invested pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy guidelines are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The City's Comprehensive Annual Financial Report categorizes the level of custodial risk associated with its pooled cash and investments, which includes \$174,039 and \$155,905 of the Program's total deposits and investments with the City Treasury as of June 30, 2000 and 1999, respectively. The City Treasury allocates monthly income from the investment of pooled cash in proportion to the Program's end-of-month balances.

The Program is required by its bond indentures to maintain certain revenue bond funds in government obligations, time deposits, or demand deposits. The Program follows the investment policy guidelines of the City Treasurer for its other investments, including those investments held by trustees.

The Program's investments, including those held by trustees, are categorized below to give an indication of the level of custodial risk assumed at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the Program or its agent in the name of the Program. Category 2 includes uninsured and unregistered investments for which the securities are held by the counter-party's trust department or agent in the name of the Program. Category 3 includes uninsured and unregistered investments for which the securities are held by the counter-party, or by its trust department or agent but not in the name of the Program.

The Program's investment portfolio is stated at fair value (except for money market funds which are stated at amortized cost, which approximates market) and is based on quotes obtained from national exchanges as of June 30, 2000 and 1999.

| | Category | | | Carrying |
|---|------------------|----------|----------|-------------------|
| | 1 | 2 | 3 | value |
| U.S. Treasury bills | \$ 13,254 | — | — | 13,254 |
| Other U.S. government securities | 26,486 | — | — | 26,486 |
| | <u>\$ 39,740</u> | <u>—</u> | <u>—</u> | 39,740 |
| Money market funds | | | | 1,530 |
| Certificate of deposit | | | | 7,000 |
| Pooled cash and investments held by the City Treasurer | | | | <u>174,039</u> |
| | | | | <u>\$ 222,309</u> |

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(5) Fixed Assets

A summary of changes in fixed assets follows:

| | Balance June 30, 1999 | Additions | Deletions and transfers | Balance June 30, 2000 |
|-----------------------------|--------------------------|-----------------|----------------------------|--------------------------|
| Land | \$ 22,192 | 253 | — | 22,445 |
| Facilities and improvements | 1,837,875 | 19,758 | — | 1,857,633 |
| Machinery and equipment | 18,224 | 314 | — | 18,538 |
| Accumulated depreciation | <u>(492,266)</u> | <u>(38,169)</u> | <u>—</u> | <u>(530,435)</u> |
| | 1,386,025 | (17,844) | — | 1,368,181 |
| Construction-in-progress | <u>8,805</u> | <u>2,769</u> | <u>—</u> | <u>11,574</u> |
| Total | <u>\$ 1,394,830</u> | <u>(15,075)</u> | <u>—</u> | <u>1,379,755</u> |

During the years ended June 30, 2000 and 1999, the Program incurred total interest cost of \$33,161 and \$34,904, respectively. Of the total amount of interest cost incurred, \$1,259 and \$1,308 was capitalized into the cost of constructing proprietary fixed assets during the years ended June 30, 2000 and 1999, respectively.

During fiscal years 2000 and 1999, the Program expensed \$7,435 and \$3,300, respectively, related to capitalized design and planning costs on certain projects which were discontinued. The amount of the write-off was recognized as other operating expense in the accompanying financial statements.

(6) Restricted Assets

Pursuant to the Clean Water Resolutions, all revenue of the Program (except amounts on deposit in the rebate fund) are irrevocably pledged to the punctual payment of debt service on the Sewer Revenue and Refunding Bonds. Accordingly, the revenue of the Program shall not be used for any other purpose while any of its Sewer Revenue and Refunding Bonds are outstanding except as expressly permitted by the Clean Water Resolutions. Further, all revenues shall be deposited by the City Treasurer in special funds designated as the Sewer Service Revenue Fund (the Sewer Revenue Fund), which must be maintained in the City Treasury. Deposits in the Sewer Revenue Fund, including earnings thereon, shall be appropriated, transferred, expended, or used for the following purposes pertaining to the financing, maintenance and operation of the Program in accordance with the following priority:

1. The payment of State loans.
2. The payment of maintenance and operation costs of the Program.
3. The payment of fees and expenses of the Fiscal Agent and payment of the periodic fees, if any, payable to any Reserve Provider or Credit Provider in conjunction with the Bonds.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

4. The payment of amounts required to be deposited into the Principal Fund, Interest Fund, Bond Reserve Fund, Sinking Fund Accounts, and any other mandatory funds and accounts created to secure Bonds issued by the City for the financing or the refinancing of the acquisition, construction or extension of the Program.
5. The payment of, or deposit into, the debt service, reserve and other mandatory funds and accounts created to secure obligations of the City payable from net revenues for the financing or refinancing of the Program which are subordinated to the Bonds.
6. Any deposits required to be made into the Repair and Replacement Fund pursuant to the Clean Water Resolutions.
7. Any deposit to be made into the Working Capital Fund pursuant to the Clean Water Resolutions.
8. Any deposit to be made into the Rate Stabilization Fund pursuant to the Clean Water Resolutions.
9. Any deposit to be made into the Surplus Revenue Fund pursuant to the Clean Water Resolutions.

In accordance with the Clean Water Resolutions, the Program maintains certain restricted cash and investment balances in trust. Restricted assets held in trust consisted on the following as of June 30:

| | <u>2000</u> | <u>1999</u> |
|---|--------------------------|-----------------------|
| Equity in deposits and investments of the City Treasurer: | | |
| Sewer Bond Construction Fund | \$ <u>122,739</u> | <u>110,884</u> |
| Total | <u>122,739</u> | <u>110,884</u> |
| Investments held by trustee: | | |
| 1991 Sewer Revenue Bond Fund | 3,003 | 2,885 |
| 1992 Sewer Revenue Refunding Bond Fund | 19,919 | 19,385 |
| 1994 Sewer Revenue Refunding Bond Fund | 16,819 | 15,858 |
| 1995 Sewer Revenue Bond Fund | <u>1,529</u> | <u>1,442</u> |
| Total | <u>41,270</u> | <u>39,570</u> |
| Interest receivable: | | |
| Sewer Bond Construction Fund | <u>1,173</u> | <u>2,022</u> |
| Total | <u>1,173</u> | <u>2,022</u> |
| Total restricted assets | \$ <u><u>165,182</u></u> | <u><u>152,476</u></u> |

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(7) Long-Term Debt

Long-term debt consisted of the following as of June 30, 2000:

| | Interest rates | Final maturity date | 1999 | Additional obligation and interest accretion | Current maturities, retirements and net decreases | 2000 |
|--|-------------------|---------------------------|------------|---|---|----------|
| Revenue Bonds: | | | | | | |
| 1991 Sewer Revenue Bonds | 5.75%-6.50% | 2003 | \$ 12,980 | — | (2,945) | 10,035 |
| 1992 Sewer Revenue Refunding Bonds | 5.50%-6.00% | 2016 | 264,820 | — | (16,515) | 248,305 |
| 1994 Sewer Revenue Refunding Bonds | 4.70%-5.80% | 2023 | 174,980 | — | (475) | 174,505 |
| 1995A Sewer Revenue Bonds | 5.38%-5.95% | 2026 | 44,230 | — | (775) | 43,455 |
| 1995B Sewer Revenue Bonds | 5.55%-5.95% | 2011 | 14,157 | 826 | — | 14,983 |
| Unamortized bond discount and refunding loss | | | (16,394) | — | 833 | (15,561) |
| Total revenue bonds | | | 494,773 | 826 | (19,877) | 475,722 |
| Less current portion of revenue bonds | | | (20,710) | — | (1,565) | (22,275) |
| Long-term portion of revenue bonds | | | \$ 474,063 | 826 | (21,442) | 453,447 |

The payments of principal and interest amounts on various bonds are collateralized by future sewer and water revenues.

(a) General Purpose Sewer Revenue Bonds Series 1991

In July 1991, the Board of Supervisors of the City adopted resolutions providing for the issuance of \$170,000 General Purpose Sewer Revenue Bonds (Series 1991). Interest rates for the issue vary from 5.75% to 6.50%.

The Series 1991 Bonds did not require voter approval as the bonds were to be used to finance facilities under Cease and Desist Orders from the San Francisco Bay Regional Water Quality Control Board (the Regional Board). The bonds are payable solely from pledged revenues of the Program and are not payable from any other source.

On March 2, 1994 Sewer Revenue Refunding Bonds Series 1994 were issued with a face value of approximately \$175,000 of which net proceeds were used to refund approximately \$144,700 of the Series 1991 Bonds in a legal defeasance (note 7c).

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

(b) *Sewer Revenue Refunding Bonds Series 1992*

On August 4, 1992, the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Refunding Bonds Series 1992 (the 1992 Refunding Bonds) in the principal amount of approximately \$331,000 with interest rates varying from 5.5% to 6.0% maturing serially through October 1, 2015.

(c) *Sewer Revenue Refunding Bonds Series 1994*

On January 24, 1994, the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Refunding Bonds Series 1994 (the 1994 Refunding Bonds) in the principal amount of \$174,980 with interest rates varying from 4.70% to 5.80%. Interest-only payments are due semi-annually on April 1 and October 1 of each year until April 1, 2000, at which time the bonds begin to mature serially through October 1, 2022.

(d) *Sewer Revenue Bonds Series 1995*

On November 8, 1994, voters approved the issuance of Sewer Revenue Bonds in the amount of approximately \$146,100. On May 8, 1995, the Board of Supervisors of the City adopted a resolution providing for the issuance of the Sewer Revenue Bonds Series 1995A and 1995B (the 1995 Bonds). The Series 1995A Bonds have a principal amount of approximately \$44,200 with interest varying from 5.38% to 5.95% and mature serially through October 1, 2025. Interest payments are due semiannually on April 1 and October 1 of each year. The Series 1995B Bonds have a principal amount of approximately \$11,300 with interest varying from 5.55% to 5.95% and mature serially from October 1, 2006 through October 1, 2010. Interest payments are due semi-annually beginning October 1, 2006 through October 1, 2010. The Program recognizes annual interest expense on the Series 1995B Bonds over the life of the Bonds using the interest method. The Program has recognized approximately \$3,700 and \$2,900 of unpaid interest on the Series 1995B Bonds as of June 30, 2000 and 1999, respectively, and has included it with the outstanding principal balance of the Series 1995B Bonds. The Series Revenue Bonds were issued for the purpose of providing funds for certain improvements to the City's sewage treatment and disposal system.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(e) Future Annual Debt Service of Revenue Bonds

The future annual debt service relating to the Revenue Bonds outstanding as of June 30, 2000 is as follows:

| | <u>Principal</u> | <u>Interest</u> |
|--|--------------------------|--------------------------|
| Year ending June 30: | | |
| 2001 | \$ 22,275 | 26,659 |
| 2002 | 23,555 | 25,442 |
| 2003 | 24,930 | 24,153 |
| 2004 | 20,415 | 22,970 |
| 2005 | 21,595 | 21,893 |
| Thereafter | <u>378,513</u> | <u>169,542</u> |
| | 491,283 | \$ <u><u>290,659</u></u> |
| Less: | | |
| Current portion | (22,275) | |
| Unamortized bond discount and refunding loss | <u>(15,561)</u> | |
| Long-term portion as of June 30, 2000 | \$ <u><u>453,447</u></u> | |

As defined in the Clean Water Resolutions, the principal and interest of the Program's Revenue and Refunding Bonds are payable from its corresponding revenue as well as monies deposited in certain funds and accounts pledged thereto (note 6).

The Program has complied with the debt covenants of the Revenue Bonds.

(8) State Revolving Fund Loans

The following is a summary of changes in state revolving fund loans for the years ended June 30, 2000:

| | <u>June 30, 1999</u> | <u>Additional obligations and interest accretion</u> | <u>Current maturities retirements, and net decreases</u> | <u>June 30, 2000</u> |
|-------------------------------------|--------------------------|--|--|--------------------------|
| State of California revolving loans | \$ <u>167,730</u> | <u>23,700</u> | <u>(11,135)</u> | <u>180,295</u> |

For the year ended June 30, 2000, the City has received two loans in the amount of \$23,700. Of that amount, \$12,000 is added to the Rankin Street Pump Station Loan, and \$11,700 is added to the Islais Creek Loan.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

The Program maintains several contracts with the California State Water Resources Board (SWRCB) under which the Program can borrow up to prescribed maximum amounts to finance the construction of certain facilities. Loans outstanding as of June 30, 2000 are summarized as follows:

| Project | Date of loan | Maturity date | Interest rate | Amount outstanding | Maximum loan amount |
|--------------|--------------|---------------|---------------|--------------------|---------------------|
| Oceanside | 07/25/90 | 2010 | 3.4% | \$ 24,900 | 40,000 |
| Oceanside | 06/10/91 | 2011 | 3.5% | 20,165 | 32,376 |
| Mariposa | 01/10/91 | 2011 | 3.5% | 4,781 | 7,624 |
| Oceanside | 04/28/92 | 2007 | 3.5% | 22,178 | 42,200 |
| Mariposa | 11/01/91 | 2011 | 3.1% | 1,300 | 1,936 |
| Lake Merced | 02/05/92 | 2012 | 3.1% | 14,151 | 21,114 |
| Islais Creek | 10/08/92 | 2012 | 3.0% | 4,052 | 5,706 |
| Oceanside | 12/24/93 | 2012 | 2.9% | 10,760 | 14,100 |
| Islais Creek | 09/07/93 | 2012 | 3.1% | 20,272 | 26,800 |
| Islais Creek | 06/17/94 | 2013 | 2.9% | 12,264 | 15,000 |
| Islais Creek | 06/13/96 | 2015 | 3.4% | 20,214 | 21,700 |
| Rankin Pump | 12/23/96 | 2016 | 2.8% | 25,258 | 27,000 |
| | | | | <u>\$ 180,295</u> | <u>255,556</u> |

The Program is repaying the interest and principal by installments with the final amount due from 15 to 20 years after the first disbursement by SWRCB. Disbursements are made by SWRCB as funds are spent for the projects. The Program is required to comply with applicable federal and state regulations. The future annual debt service relating to the State Revolving Fund Loans outstanding as of June 30, 2000 is as follows:

| | Principal | Interest |
|---------------------------------------|-------------------|-------------------|
| Year ending June 30: | | |
| 2001 | \$ 12,998 | 18,381 |
| 2002 | 13,018 | 18,381 |
| 2003 | 13,443 | 18,381 |
| 2004 | 13,883 | 18,381 |
| 2005 | 14,337 | 18,381 |
| Thereafter | <u>112,616</u> | <u>129,890</u> |
| | 180,295 | \$ <u>221,795</u> |
| Less current portion | <u>12,998</u> | |
| Long-term portion as of June 30, 2000 | <u>\$ 167,297</u> | |

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(9) Deferred Revenue

In January 1995, the Program entered into a forward purchase and sale agreement with an investment bank (the Bank). Under the agreement, the Program received an upfront fee of approximately \$8,900 from the Bank. In exchange, the Program will use its debt service payments deposited but not yet due to bondholders to purchase short-term U.S. Treasury bills from the Bank at face value.

The upfront fee was deposited into the Program's Rate Stabilization Fund and recorded as deferred revenue in the accompanying financial statements. Revenue is being recognized over the life of the agreement based on the present value of the future earnings. The unamortized balance as of June 30, 2000 and 1999 is approximately \$3,300 and \$4,300, respectively.

(10) Employee Benefits

(a) Retirement Plan

Plan Description—The City has a single-employer defined benefit retirement plan (the Plan) which is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). The Plan covers substantially all full-time employees of the Program along with other employees of the City. The Plan provides basic service retirement, disability and death benefits based on specified percentages of final average salary and provides cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to San Francisco City and County Employees' Retirement System, 30 Van Ness Avenue, Suite 3000, San Francisco, CA 94102, or by calling (415) 487-7020.

Funding Policy—Contributions are made to the basic plan by both the Program and its employees. Employee contributions are mandatory. Employee contribution rates for 2000 and 1999 were between 7% and 8% as a percentage of covered payroll. The Program is required to contribute at an actuarially determined rate. No Program contributions were required for 2000 and 1999 as the actuarially determined contribution rate as a percentage of covered payroll was 0%. The Program's contributions to the Retirement System on behalf of its employees amounted to \$1,460, \$1,336 and \$1,201 for the years ended June 30, 2000, 1999, and 1998, respectively, which was equal to the required employee contributions for those years.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(b) Health Care Benefits

Health care benefits of Program employees, retired employees and surviving spouses are financed by beneficiaries and the City through the City and County of San Francisco Health Service System, an internal service fund. The Program's contributions covering current and retired employees, which amounted to approximately \$1,658 and \$1,300 in fiscal years 2000 and 1999, respectively, are determined by Charter provisions based on similar contributions made by the ten most populous counties in California. The Program's liability for both current employee and postretirement health care benefits is limited to its annual contribution.

(11) Related Parties

Certain administrative costs of the Commission are allocated to the Program. For the years ended June 30, 2000 and 1999, the Commission allocated \$10,402 and \$9,283, respectively, in administrative costs to the Program.

The City performs certain administrative services such as maintenance of accounting records and investment of cash for all fund groups within the City. The various funds are charged for these services based on the City's indirect cost allocation plan. The overhead allocation paid to the General Fund of the City by the Program was \$1,784 and \$1,735 for the years ended June 30, 2000 and 1999, respectively, and is included in other operating expenses in the accompanying financial statements.

The Program purchases electricity from the Hetch Hetchy Project at market rates. This amount, totaling \$5,650 and \$5,701 for the years ended June 30, 2000 and 1999, respectively, has been included in services provided by other departments in the accompanying financial statements.

The Program provides sewer services to other City departments at the nonresidential rates established by the Program.

The SFWD bills and collects sewer service charges on behalf of the Program.

The City's Department of Public Works (DPW) provides certain engineering and other services to the Program and charges amounts designed to recover its costs. This amount totaling approximately \$8,350 and \$10,500 for the years ended June 30, 2000 and 1999, respectively, has been included in services provided by other departments in the accompanying financial statements.

A variety of other City departments provides services such as purchasing, legal, data processing, telecommunications and human resources to the Program and charges amounts designed to recover those departments' costs. These charges totaling approximately \$2,044 and \$4,100 for the years ended June 30, 2000 and 1999, respectively, have been included in services provided by other departments in the accompanying financial statements.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(12) Risk Management

The Program is self-insured for general liabilities, property damage and workers' compensation claims. The risk of loss is managed internally by setting aside assets for claim settlement and recording a liability representing an estimate of the cost of all outstanding claims and incurred but not reported claims. Claim liabilities are recorded when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount and, therefore, it is reasonably possible that claim liabilities could change in the future. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and legal factors. The liabilities have been actuarially determined. Changes in the reported liability for the years ended June 30, 2000 and 1999 resulted from the following:

| | <u>2000</u> | <u>1999</u> |
|--|-----------------|----------------|
| Beginning of year liability | \$ 2,443 | 6,925 |
| Current year claims and changes in estimates | 745 | 1,637 |
| Current year claims payments | <u>(1,196)</u> | <u>(6,119)</u> |
| End of year liability | <u>\$ 1,992</u> | <u>2,443</u> |
| Damage and claims liability | \$ 433 | 1,310 |
| Accrued workers' compensation | <u>1,559</u> | <u>1,133</u> |
| | <u>\$ 1,992</u> | <u>2,443</u> |

(13) Commitments, Litigation and Contingencies

(a) Commitments

As of June 30, 2000 and 1999, the Program has outstanding commitments with third parties of \$16,500 for various capital projects and other purchase agreements for materials and services.

(b) Grants

Grants that the Program receives are subject to audit and final acceptance by the granting agency. Current and prior year costs of such grants are subject to adjustment upon audit.

SAN FRANCISCO CLEAN WATER PROGRAM

Notes to Financial Statements

June 30, 2000 and 1999

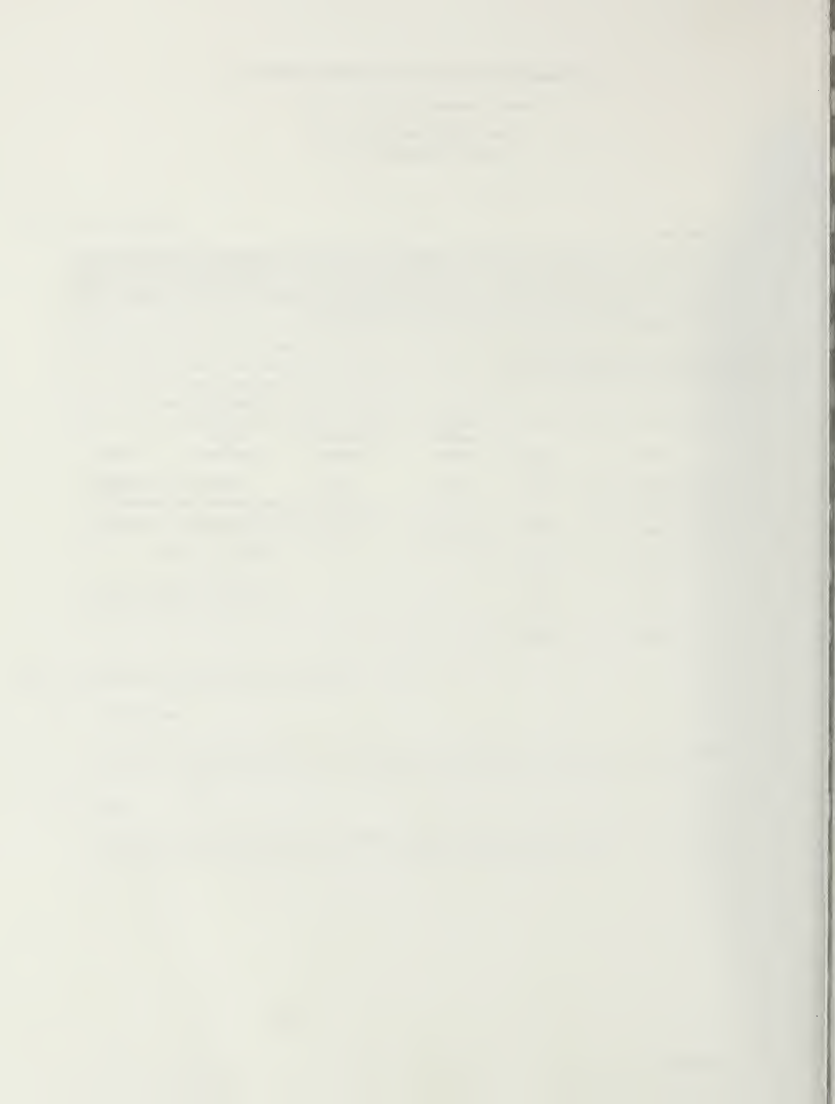
(dollars in thousands)

(c) *Litigation*

The Program is a defendant in various legal actions and claims that arise during the normal course of business. The final disposition of these legal actions and claims is not determinable; however, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or results of operations of the Program.

(14) Reconciliation of Contributed Capital

| | | Federal capital grants | State capital grants | Contribution from City and County of San Francisco | Total |
|------------------------------------|----|---------------------------------------|---------------------------------|---|--------------|
| Contributed capital, June 30, 1999 | \$ | 432,561 | 67,165 | 108,238 | 607,964 |
| Allocation of depreciation | | (11,112) | (1,649) | — | (12,761) |
| Contributed capital, June 30, 2000 | \$ | 421,449 | 65,516 | 108,238 | 595,203 |



SAN FRANCISCO WATER DEPARTMENT

Financial Statements

June 30, 2000 and 1999

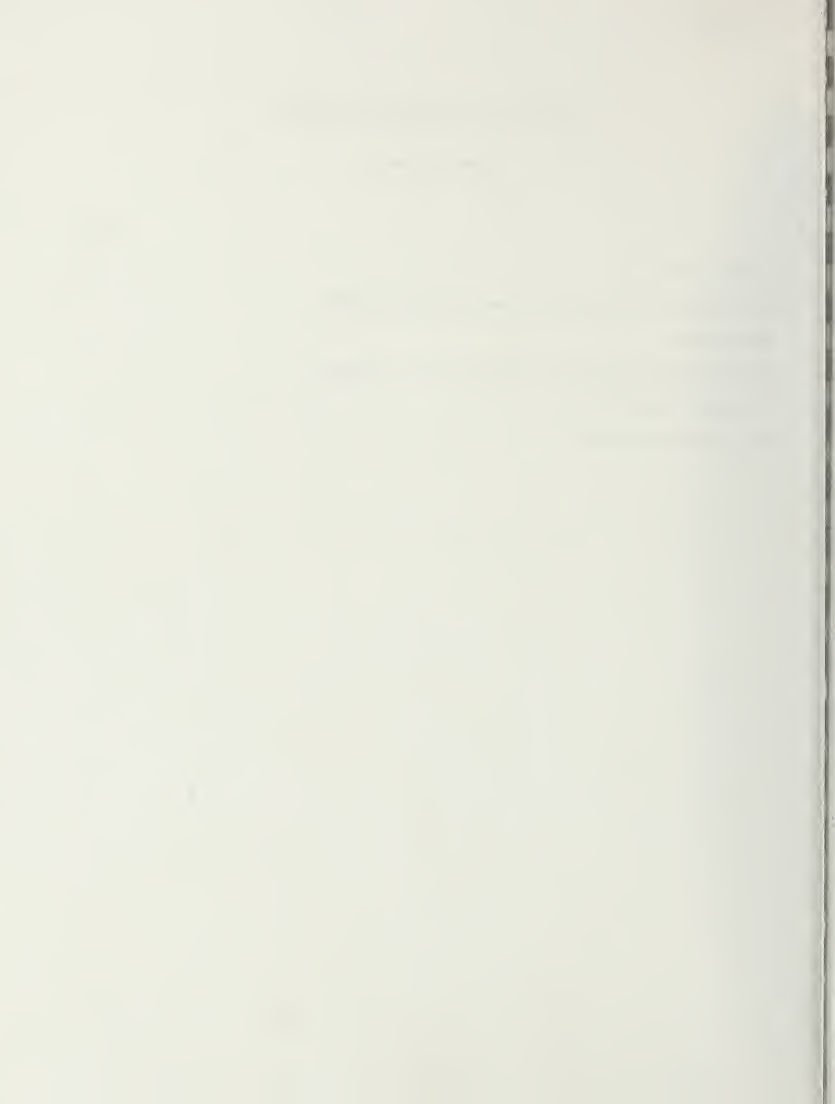
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SAN FRANCISCO WATER DEPARTMENT

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Three Embarcadero Center
San Francisco, CA 94111

Independent Auditors' Report

Honorable Mayor and Board of Supervisors
City and County of San Francisco, California:

We have audited the accompanying financial statements of the San Francisco Water Department (the Department) of the City and County of San Francisco, California (the City), as of and for the years ended June 30, 2000 and 1999, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 1, the financial statements referred to above present only the financial activities of the Department and are not intended to present fairly the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the San Francisco Water Department of the City and County of San Francisco, California, as of June 30, 2000 and 1999, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

October 25, 2000



KPMG LLP KPMG LLP a U.S. limited liability partnership
a member of KPMG International, a Swiss association

SAN FRANCISCO WATER DEPARTMENT

Balance Sheets

June 30, 2000 and 1999
(in thousands)

| Assets | 2000 | 1999 |
|--|------------|---------|
| Current assets: | | |
| Deposits and investments with City Treasury | \$ 77,134 | 64,750 |
| Deposits and investments outside City Treasury | 40 | 67 |
| Receivables: | | |
| Charges for services (net of allowance for doubtful accounts of \$982 in 2000 and 1999) | 9,412 | 8,834 |
| Suburban water rate agreement | 2,457 | 5,807 |
| Interest and other | 1,746 | 1,728 |
| Total receivables | 13,615 | 16,369 |
| Inventories | 1,000 | 802 |
| Total current assets | 91,789 | 81,988 |
| Restricted assets: | | |
| Deposits and investments with City Treasury | 45,414 | 56,858 |
| Deposits and investments outside City Treasury | 10,139 | 9,655 |
| Interest receivable | 1,066 | 1,291 |
| Total restricted assets | 56,619 | 67,804 |
| Fixed assets, net of accumulated depreciation | 461,798 | 429,755 |
| Bond issuance costs (net of accumulated amortization of \$1.199 in 2000 and \$1.086 in 1999) | 1,833 | 1,925 |
| Total assets | \$ 612,039 | 581,472 |
| Liabilities and Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 5,166 | 3,920 |
| Accrued payroll | 5,026 | 3,634 |
| Accrued vacation and sick leave, current portion | 2,977 | 2,863 |
| Accrued workers' compensation, current portion | 964 | 810 |
| Damage and claims liability, current portion | 2,080 | 739 |
| Deposits, advances and other liabilities | 12,509 | 2,441 |
| Bond interest payable | 2,317 | 2,288 |
| General obligation bonds, current portion | — | 830 |
| Revenue bonds, current portion | 6,955 | 6,585 |
| Commercial paper | 20,000 | — |
| Total current liabilities | 57,994 | 24,110 |
| Liabilities payable from restricted assets | 3,850 | 1,489 |
| Long-term liabilities: | | |
| Accrued vacation and vested sick leave | 3,048 | 3,221 |
| Accrued workers' compensation | 2,733 | 2,245 |
| Damage and claims liability | 11,300 | 2,705 |
| Revenue bonds | 222,262 | 228,683 |
| Total long-term liabilities | 239,343 | 236,854 |
| Total liabilities | 301,187 | 262,453 |
| Equity: | | |
| Contributed capital | 75 | 75 |
| Retained earnings - reserved for bond requirements and other commitments | 5,038 | 7,169 |
| Retained earnings - unreserved | 305,739 | 311,775 |
| Total retained earnings | 310,777 | 318,944 |
| Total equity | 310,852 | 319,019 |
| Total liabilities and equity | \$ 612,039 | 581,472 |

See accompanying notes to financial statements.

SAN FRANCISCO WATER DEPARTMENT

Statements of Revenues, Expenses, and Changes in Retained Earnings

Years ended June 30, 2000 and 1999

(in thousands)

| | 2000 | 1999 |
|---|------------|----------|
| Operating revenues: | | |
| Charges for services | \$ 132,551 | 128,347 |
| Rents and concessions | 7,881 | 7,201 |
| Other revenue | 3,788 | 3,028 |
| Total operating revenues | 144,220 | 138,576 |
| Operating expenses: | | |
| Personal services | 50,523 | 44,570 |
| Contractual services | 6,757 | 6,991 |
| Materials and supplies | 8,055 | 7,019 |
| Depreciation | 22,974 | 20,195 |
| Bad debts | — | 190 |
| Services provided by other departments | 29,686 | 28,825 |
| General and administrative | 26,995 | 16,530 |
| Other | 4,416 | 1,369 |
| Total operating expenses | 149,406 | 125,689 |
| Operating (loss) income | (5,186) | 12,887 |
| Nonoperating revenues (expenses): | | |
| Federal | — | 615 |
| State/other | 26 | 110 |
| Interest and investment income | 8,632 | 6,929 |
| Interest expense | (13,040) | (13,511) |
| Other nonoperating revenues, net | 1,401 | 4,720 |
| Net nonoperating expenses | (2,981) | (1,137) |
| (Loss) income before operating transfers | (8,167) | 11,750 |
| Operating transfers from the City and County of San Francisco | 849 | 1,406 |
| Operating transfers to the City and County of San Francisco | (849) | (1,696) |
| Net operating transfers | — | (290) |
| Net (loss) income | (8,167) | 11,460 |
| Retained earnings at beginning of year | 318,944 | 307,484 |
| Retained earnings at end of year | \$ 310,777 | 318,944 |

See accompanying notes to financial statements.

SAN FRANCISCO WATER DEPARTMENT

Statements of Cash Flows

Years ended June 30, 2000 and 1999
(in thousands)

| | <u>2000</u> | <u>1999</u> |
|---|------------------|-----------------|
| Cash flows from operating activities: | | |
| Cash received from customers, including cash deposits | \$ 139,702 | 118,055 |
| Cash received from tenants for rent | 7,881 | 7,502 |
| Cash paid to employees for services | (49,190) | (43,339) |
| Cash paid to suppliers for goods and services | (18,180) | (13,692) |
| Cash paid for judgments and claims | (2,106) | (3,830) |
| Cash paid for quasi-external transactions | (43,997) | (44,567) |
| Net cash provided by operating activities | <u>34,110</u> | <u>20,129</u> |
| Cash flows from noncapital financing activities: | | |
| Operating grants | 26 | 544 |
| Operating transfers in | 849 | 1,406 |
| Operating transfers out | (849) | (1,696) |
| Net cash provided by noncapital financing activities | <u>26</u> | <u>254</u> |
| Cash flows from financing activities: | | |
| Proceeds from sale of fixed assets | 9,967 | 3,549 |
| Proceeds from commercial paper borrowings | 20,000 | — |
| Interest paid on long-term debt | (14,012) | (13,918) |
| Principal paid on long-term debt | (7,415) | (6,440) |
| Acquisition and construction of capital assets | (51,448) | (39,504) |
| Net cash used in financing activities | <u>(42,908)</u> | <u>(56,313)</u> |
| Cash flows from investing activities: | | |
| Interest income received | 9,267 | 6,350 |
| Proceeds from sale of investments | 20,074 | 18,912 |
| Purchase of investments | (20,558) | (18,995) |
| Purchase of restricted deposits and investments | (25,000) | (91,270) |
| Proceeds from sale or restricted deposits and investments | 40,458 | 66,487 |
| Other investing activities | 1,453 | 1,613 |
| Net cash provided by (used in) investing activities | <u>25,694</u> | <u>(16,903)</u> |
| Increase (decrease) in cash and cash equivalents | <u>16,922</u> | <u>(52,833)</u> |
| Cash and cash equivalents: | | |
| Beginning of year | <u>81,755</u> | <u>134,588</u> |
| End of year | <u>\$ 98,677</u> | <u>81,755</u> |

SAN FRANCISCO WATER DEPARTMENT

Statements of Cash Flows

Years ended June 30, 2000 and 1999
(in thousands)

| | 2000 | 1999 |
|--|------------|----------|
| Reconciliation of operating (loss) income to net cash provided by operating activities: | | |
| Operating (loss) income | \$ (5,186) | 12,887 |
| Adjustments to reconcile operating (loss) income to net cash provided by operating activities: | | |
| Depreciation and amortization | 22,974 | 20,195 |
| Provision for uncollectible accounts | — | 190 |
| Changes in assets and liabilities: | | |
| Receivables: | | |
| Charges for services, net | (805) | 301 |
| Suburban water rate agreement | 3,350 | (5,807) |
| Other | 350 | (335) |
| Inventories | (198) | (20) |
| Accounts payable | 1,246 | 356 |
| Accrued payroll | 1,392 | 696 |
| Accrued vacation and vested sick leave | (59) | 535 |
| Accrued workers' compensation | 642 | 705 |
| Suburban water rate agreement liability | — | (7,370) |
| Damage and claims liability | 9,936 | (2,396) |
| Deposits, advances and other liabilities | 468 | 192 |
| Net cash provided by operating activities | \$ 34,110 | 20,129 |
| Reconciliation of cash and cash equivalents to the balance sheet: | | |
| Deposits and investments with City Treasury: | | |
| Unrestricted | \$ 77,134 | 64,750 |
| Restricted | 45,414 | 56,858 |
| Deposits and investments outside City Treasury – unrestricted | 40 | 67 |
| Total deposits and investments | 122,588 | 121,675 |
| Less deposits and investments not meeting the definition of cash equivalents | (23,911) | (39,920) |
| Cash and cash equivalents at end of year on statements of cash flows | \$ 98,677 | 81,755 |

See accompanying notes to financial statements.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(1) The Financial Reporting Entity

The San Francisco Water Department (the Department) was established in 1930 under the provisions of the City Charter of San Francisco. The Department acquired the fully developed, mature water works for San Francisco on March 3, 1930. Since then, the City and County of San Francisco (the City) has operated and maintained the water works as the San Francisco Water Department. The Board of Supervisors of the City has adopted resolutions (the Water Resolutions) providing for the issuance of various water revenue and refunding bond series. The Department, which consists of a system of reservoirs, storage tanks, water treatment plants, pump stations, and pipelines, is engaged in the distribution of water to San Francisco and certain suburban areas. On average, the Department delivers 92,752 million gallons of water annually to nearly 2.4 million people within San Francisco and certain suburban areas.

The San Francisco Public Utilities Commission (the Commission), established in 1932, is responsible for providing operational oversight of the public utility enterprises of the City, which include the Department along with the City's power and sewer utilities (e.g., Hetch Hetchy Water and Power [Hetch Hetchy] and the San Francisco Clean Water Program). The Commission consists of five members appointed by the Mayor, who are responsible for determining such matters as the rates and charges for services, approval of contracts, and organizational policy. The Commission is a department of the City and, as such, the financial operations of the Department, Hetch Hetchy, and the San Francisco Clean Water Program are included in the Comprehensive Annual Financial Report of the City as enterprise funds. These financial statements present only the financial operations of the Department and are not intended to present the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types.

(2) Significant Accounting Policies

(a) *Basis of Accounting—Fund Accounting*

The accounts of the Department are organized on the basis of a proprietary fund type, specifically an enterprise fund. The operations of this fund are accounted for with a separate set of self-balancing accounts that comprise the Department's assets, liabilities, fund equity, revenues, and expenses. Enterprise Funds account for operations (i) that are financed and operated in a manner similar to private business enterprises where the intent of the Commission is that the Department's costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (ii) where the Commission has decided that periodic determination of revenues earned, expenses incurred, and net income or loss of the Department is appropriate for capital maintenance, public policy, management control, accountability, or other purpose.

(b) *Measurement Focus*

The financial activities of the Department are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Under this method, all assets and liabilities associated with its operations are included on the balance sheet; revenues are recorded when earned, and expenses are recorded when liabilities are incurred.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

The Department does not apply Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989. The Department applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as statements and interpretations of the FASB, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

(c) Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid investments, including restricted assets, with an original purchased maturity of three months or less.

(d) Investments

Certain investments are stated at fair value based on quoted market prices. Changes in fair value are recognized as investment income.

Money market funds and banker's acceptances that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost.

(e) Inventory

Inventory primarily consists of construction materials and maintenance supplies, and is generally valued at cost or average cost. Inventory is expensed as it is consumed.

(f) Fixed Assets

Fixed assets are stated at cost. Depreciation is computed using the straight-line method based on the estimated useful lives of the related assets, which range from 3 to 75 years for equipment and 3 to 173 years for buildings, structures, and improvements. No depreciation is recorded in the year of acquisition, and a full year's depreciation is recorded in the year of disposal.

(g) Construction in Progress

The cost of acquisition and construction of major plant and equipment is recorded as construction in progress. As facilities are accepted by the Department and become operative, they are transferred to the plant and equipment accounts and depreciated in accordance with the Department's depreciation policies. Costs of construction projects that are discontinued are recorded as expense in the year in which the decision is made to discontinue such projects.

(h) Capitalization of Interest

A portion of the interest cost incurred on capital projects is capitalized on assets that require a period of time for construction or to otherwise prepare them for their intended use. Such amounts are amortized over the useful lives of the assets.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(i) ***Bond Discount and Issuance Costs***

Bond discount and issuance costs are amortized over the term of the related bonds.

(j) ***Accrued Vacation, Sick Leave***

Accrued vacation pay, which may be accumulated up to ten weeks per employee, is charged to expense as earned. Unused sick leave accumulated through December 6, 1978 is vested and payable upon termination of employment by retirement, death, or disability caused by industrial accident. Sick leave earned subsequent to that date is nonvesting and may be accumulated up to six months per employee.

(k) ***Workers' Compensation***

The Department is self-insured for workers' compensation claims and accrues the estimated cost of those claims, including the estimated cost of incurred but not reported claims.

(l) ***Damage and Claims Liability***

The Department is self-insured for general liability and property damage claims. The liability represents an estimate of the cost of all outstanding claims, including adverse loss development, and estimated incurred but not reported claims.

(m) ***Arbitrage Rebate Payable***

Certain bonds are subject to arbitrage rebate requirements in accordance with regulations issued by the U.S. Treasury Department. The requirements generally stipulate that earnings from the investment of the tax-exempt bond proceeds that exceed related interest costs on the bonds must be remitted to the federal government on every fifth anniversary of each bond issue. The arbitrage rebate liability was \$496 and \$441 as of June 30, 2000 and 1999, respectively, and is included in accounts payable in the accompanying balance sheet.

(n) ***Refunding of Debt***

Gains or losses occurring from advance refundings of debt are deferred and amortized into interest expense over the remaining life of the old bonds or the life of the new bonds, whichever is shorter.

(o) ***Income Taxes***

As a government agency, the Department is exempt from both federal income taxes and California state franchise taxes.

(p) ***Revenue Recognition***

Revenues from water services furnished to consumers are recorded in the financial statements in the period that meters are read. In general, customers are billed on a cyclical basis with large commercial and industrial customers billed monthly, and all other customers bimonthly.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

In June 1998, the voters passed Proposition H, which effectively froze the water rates at the levels in effect as of January 1, 1998 until July 1, 2006, subject to certain limitations such as to service pre-existing debt. The passage of Proposition H limits the Department's ability to fund future water system maintenance projects and/or meet new federal and state regulations that may arise during the period in which Proposition H is effective.

(g) *Use of Estimates*

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(r) *Reclassifications*

Certain reclassifications have been made to the 1999 financial statements to conform to the 2000 presentation. These reclassifications did not change total assets, liabilities, equity, or net income.

(3) **Reserved Retained Earnings**

Calculation of reserved retained earnings as of June 30, 2000 (in thousands) is as follows:

Restricted assets:

| | | |
|--|----|--------------|
| Deposits and investments with City Treasury | \$ | 45,414 |
| Deposits and investments outside City Treasury | | 10,139 |
| Interest receivable | | <u>1,066</u> |
| Total restricted assets | | 56,619 |

Less:

| | | |
|--|--|--------------|
| Bond construction funds | | 45,414 |
| Accrued interest payable on bond proceeds | | 2,317 |
| Liabilities payable from restricted assets | | <u>3,850</u> |

| | | |
|----------------------------|----|--------------|
| Reserved retained earnings | \$ | <u>5,038</u> |
|----------------------------|----|--------------|

| | | |
|-------------------------|----|---------|
| Total retained earnings | \$ | 310,777 |
|-------------------------|----|---------|

| | | |
|---|--|--------------|
| Less reserved retained earnings as calculated above | | <u>5,038</u> |
|---|--|--------------|

| | | |
|------------------------------|----|----------------|
| Unreserved retained earnings | \$ | <u>305,739</u> |
|------------------------------|----|----------------|

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(4) Cash and Investments

The captions on the balance sheet related to cash and investments as of June 30, 2000 and 1999 are as follows:

| | <u>2000</u> | <u>1999</u> |
|---|-------------------|----------------|
| Deposits and investments with City Treasury: | | |
| Unrestricted – pooled | \$ 77,134 | 64,750 |
| Restricted – pooled and nonpooled (note 6) | 45,414 | 56,858 |
| Deposits and investments outside City Treasury: | | |
| Unrestricted | 40 | 67 |
| Restricted (note 6) | <u>10,139</u> | <u>9,655</u> |
| | <u>\$ 132,727</u> | <u>131,330</u> |

Investments

The Department's deposits and investments with the City Treasury are invested pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy guidelines are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The City's Comprehensive Annual Financial Report categorizes the level of custodial risk associated with the its pooled cash and investments, which includes \$92,548 and \$69,202 of the Department's total deposits and investments with the City Treasury as of June 30, 2000 and 1999, respectively. The City Treasurer allocates monthly income from the investment of pooled cash in proportion to the Department's end-of-month balances.

The Department is required by its bond indentures to maintain certain revenue bond funds in government obligations, time deposits, or demand deposits. The Department follows the investment policy guidelines of the City Treasurer for its other investments, including those investments held by trustees.

The Department's investments, including those held by trustees, are categorized below to give an indication of the level of custodial risk assumed at year-end. Category 1 includes investments that are insured or registered or for which the securities are held by the Department or its agent in the name of the Department. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the name of the Department. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the name of the Department.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

The Department's investment portfolio is stated at fair value (except for certificates of deposit, money market funds and banker's acceptances, which are stated at amortized cost, which approximates market). Fair value is based on quotes obtained from national exchanges as of June 30, 2000.

| | Category | | | Carrying value |
|---|------------------|----------|----------|-------------------|
| | 1 | 2 | 3 | |
| U.S. Treasury bills (fiscal agent) | \$ 10,139 | — | — | 10,139 |
| | <u>\$ 10,139</u> | <u>—</u> | <u>—</u> | 10,139 |
| Certificate of deposits | | | | 30,000 |
| Imprest funds | | | | 40 |
| Pooled cash and investments held by the City Treasurer | | | | <u>92,548</u> |
| | | | | \$ <u>132,727</u> |

(5) Fixed Assets

A summary of changes in fixed assets follows:

| | Balance June 30, 1999 | Additions | Deletions and transfers | Balance June 30, 2000 |
|-----------------------------|--------------------------|-----------------|----------------------------|--------------------------|
| Land | \$ 17,217 | — | — | 17,217 |
| Facilities and improvements | 601,426 | 26,886 | — | 628,312 |
| Machinery and equipment | 52,672 | 3,357 | (96) | 55,933 |
| Accumulated depreciation | <u>(282,230)</u> | <u>(22,974)</u> | <u>90</u> | <u>(305,114)</u> |
| | 389,085 | 7,269 | (6) | 396,348 |
| Construction-in-progress | <u>40,670</u> | <u>24,780</u> | <u>—</u> | <u>65,450</u> |
| Total | <u>\$ 429,755</u> | <u>32,049</u> | <u>(6)</u> | <u>461,798</u> |

During the years ended June 30, 2000 and 1999, the Department incurred total interest cost of \$14,248 and \$14,249, respectively. Of the total amount of interest cost incurred, \$1,208 and \$738 was capitalized into the cost of constructed assets during the years ended June 30, 2000 and 1999, respectively.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

(6) Restricted Assets

Pursuant to the Water Resolutions, all revenues of the Department (except amounts on deposit in the rebate fund) are irrevocably pledged to the punctual payment of debt service on the Water Revenue and Refunding Bonds. Accordingly, the revenues of the Department shall not be used for any other purpose while any of its Water Revenue and Refunding Bonds are outstanding, except as expressly permitted by the Water Resolutions. Further, all revenues shall be deposited by the City Treasurer in special funds designated as the Water Department Revenue Fund (the Water Revenue Fund), which must be maintained in the City Treasury. Deposits in the Water Revenue Fund, including earnings thereon, shall be appropriated, transferred, expended, or used for the following purposes pertaining to the financing, maintenance, and operation of the Department in accordance with the following priority:

1. The payment of operation and maintenance expenses for such utility and related facilities.
2. The payment of pension charges and proportionate payments to such compensation and other insurance or outside reserve funds as the Department may establish or the Board of Supervisors may require with respect to employees of the Department.
3. The payment of principal, interest, reserve, sinking fund, and other mandatory funds created to secure Revenue Bonds issued by the Department for the acquisition, construction, or extension of facilities owned, operated, or controlled by the Department.
4. The payment of principal and interest on General Obligation Bonds issued by the City for the Department's purposes.
5. Reconstruction and replacement as determined by the Department or as required by any of the Department's Revenue Bond ordinance duly adopted and approved.
6. The acquisition of land, real property, or interest in real property for, and the acquisition, construction, enlargement, and improvement of, new and existing buildings, structures, facilities, equipment, appliances, and other property necessary or convenient to the development or improvement of such utility owned, controlled, or operated by the Department; and for any other lawful purpose of the Department including the transfer of surplus funds pursuant to Section 6.407(e) of the City's Charter.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

In accordance with the Water Resolutions, the Department maintains certain restricted cash and investment balances in trust. Restricted assets held in trust consisted of the following as of June 30, 2000 and 1999:

| | <u>2000</u> | <u>1999</u> |
|---|-------------------------|----------------------|
| Equity in deposits and investments of the City Treasurer: | | |
| Water Bond Construction Fund | \$ <u>45,414</u> | <u>56,858</u> |
| Total | <u>45,414</u> | <u>56,858</u> |
| Investments held by trustee: | | |
| 1991 Water Revenue Bond Fund | 3,806 | 3,615 |
| 1992 Water Revenue Bond Fund | 3,688 | 3,486 |
| 1996 Water Revenue Bond Fund | <u>2,645</u> | <u>2,554</u> |
| Total | <u>10,139</u> | <u>9,655</u> |
| Interest receivable: | | |
| Water Bond Construction Fund | <u>1,066</u> | <u>1,291</u> |
| Total | <u>1,066</u> | <u>1,291</u> |
| Total restricted assets | \$ <u><u>56,619</u></u> | <u><u>67,804</u></u> |

(7) Commercial Paper

In November 1997, the voters approved Propositions A&B, authorizing up to \$304 million in Water Revenue Bonds to fund capital improvements for the Water Enterprise. In May and June 1999, the Public Utilities Commission and the Board of Supervisors respectively approved a commercial paper program to provide short-term financing for capital improvement projects funded under the \$304 million Water Revenue Bond Program. Under the enabling ordinance approved by the Board of Supervisors, the maximum amount of commercial paper that may be outstanding at any given time is \$150 million. As of June 30, 2000 and 1999, the amount of outstanding commercial paper is \$20 million.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(8) Long-Term Debt

Long-term debt consisted of the following as of June 30, 2000:

| | Interest rates | Due serially to | | 1999 | Additional obligation and interest accretion | Current maturities, retirements, and net decreases | 2000 |
|--|-------------------|-----------------------|----|-----------------|---|--|----------------|
| General obligation bonds: | | | | | | | |
| 1972 Municipal Water System Bonds | 4.00%-5.70% | 2000 | \$ | 830 | — | (830) | — |
| Less current portion of general obligation bonds | | | | <u>(830)</u> | <u>—</u> | <u>830</u> | <u>—</u> |
| Long-term portion of general obligation bonds | | | \$ | <u>—</u> | <u>—</u> | <u>—</u> | <u>—</u> |
| Revenue Bonds: | | | | | | | |
| 1991A Revenue Bonds | 5.30%-7.40% | 2021 | \$ | 10,354 | 130 | (1,505) | 8,979 |
| 1992A Revenue Refunding Bonds | 5.53%-6.50% | 2016 | | 103,705 | — | (3,655) | 100,050 |
| 1996A Revenue Refunding Bonds | 5.00%-6.50% | 2026 | | 131,255 | — | (1,425) | 129,830 |
| Unamortized bond discount and refunding loss | | | | <u>(10,046)</u> | <u>—</u> | <u>404</u> | <u>(9,642)</u> |
| Total revenue bonds | | | | 235,268 | 130 | (6,181) | 229,217 |
| Less current portion of revenue bonds | | | | <u>(6,585)</u> | <u>—</u> | <u>(370)</u> | <u>(6,955)</u> |
| Long-term portion of revenue bonds | | | \$ | <u>228,683</u> | <u>130</u> | <u>(6,551)</u> | <u>222,262</u> |

The payments of principal and interest amounts on various bonds are collateralized by future water revenues.

(a) General Obligation Bonds

During 1972, the Department issued \$39,000 of General Obligation Bonds relating to the municipal water system. The bonds had interest rates ranging from 4.0% to 5.7% and matured annually through fiscal year 2000.

The Department has complied with the debt covenants of the General Obligation Bonds.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(b) Water Revenue Bonds Series 1991A

During fiscal year 1991, the Department issued Revenue Bonds of approximately \$70,146 with interest varying from 5.3% to 7.4%. The Revenue Bonds include current interest serial and term bonds with an original principal amount of approximately \$92,985, and serial capital appreciation bonds with an original principal amount of approximately \$1,051. The current interest serial bonds mature through November 1, 2007, and the current interest term bonds mature on November 1, 2010, 2017 and 2020. The serial capital appreciation bonds mature from November 1, 2018 through November 1, 2019. Interest on the capital appreciation bonds is due upon maturity, and is recognized as annual interest expense over the life of the bonds using the interest method. The Department has recognized approximately \$898 and \$769 of unpaid interest on the capital appreciation bonds as of June 30, 2000 and 1999, respectively, and has included it with the outstanding principal balance of the bonds.

(c) Water Revenue Refunding Bonds Series 1992A

During fiscal year 1992, the Department issued \$107,180 of Revenue Refunding Bonds (the 1992A Refunding Bonds) pursuant to a crossover refunding of 1987 Water Revenue Refunding Bonds. The proceeds were used to purchase U.S. government securities which were placed into an irrevocable trust to be used for the payment of interest on the 1992 Refunding Bonds, and \$460 per year of principal due on the 1987 Refunding Bonds through November 1, 1997 (crossover date), at which time the remaining proceeds were used to advance refund the 1987 Refunding Bonds which amounted to \$102,570 including a call premium of \$860 and additional interest of \$1,114. The debt service requirements of the 1992 Refunding Bonds after the crossover date are being made from the net revenues of the Department.

(d) Water Revenue Refunding Bonds Series 1996A

During fiscal year 1997, the Department issued \$131,470 (face value) of 1996 Series A Water Revenue Bonds. A portion of the bond proceeds was designated for the purpose of refunding \$53,090 (face value) of 1991 Revenue Bonds which were due serially to 2020. The funding extended maturities on the bonds in order to lower required annual payments. After payment of \$852 in issue costs, \$57,012 of the net bond proceeds was transferred to a trustee to be placed in an irrevocable trust to redeem the refunded portion of the 1991 Revenue Bonds. Accordingly, the refunded portion of the 1991 Revenue Bonds was removed from the Department's balance sheet. The advance refunding decreased the Department's total debt service payment over the next 29 years by \$2,475, and provided for an economic gain of \$4,064. The resulting accounting loss of \$5,989 has been deferred and is being amortized over the remaining life of the old debt. As of June 30, 2000 and 1999, the unamortized portion of the accounting loss was \$4,817 and \$5,144 respectively.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(e) Future Annual Debt Service of Revenue Bonds

The future annual debt service relating to the Revenue Bonds outstanding as of June 30, 2000 is as follows:

| | <u>Principal</u> | <u>Interest</u> |
|---|-------------------|-------------------|
| Year ending June 30: | | |
| 2001 | \$ 6,955 | 13,108 |
| 2002 | 7,350 | 12,699 |
| 2003 | 7,775 | 12,247 |
| 2004 | 8,260 | 11,748 |
| 2005 | 8,775 | 11,215 |
| Thereafter | <u>199,744</u> | <u>94,549</u> |
| | 238,859 | \$ <u>155,566</u> |
| Less current portion | (6,955) | |
| Less unamortized bond discount and refunding loss | <u>(9,642)</u> | |
| Long-term portion as of June 30, 2000 | \$ <u>222,262</u> | |

As defined in the Water Resolutions, the principal and interest of the Department's Revenue and Refunding Bonds are payable from its corresponding revenue as well as monies deposited in certain funds and accounts pledged thereto (note 6).

The Department has complied with the debt covenants of the Revenue Bonds.

(9) Suburban Water Rate Agreement

During 1984, the City entered into a Settlement Agreement and Master Water Sales Contract (the Suburban Water Rate Agreement) with certain suburban customers, which establishes water rates to be charged to those customers (the Suburban Purchasers). Pursuant to the terms of the Suburban Water Rate Agreement, the City is required to establish water rates applicable to the Suburban Purchasers at the beginning of each fiscal year. The suburban water rates are based on an estimate of the level of revenues necessary to recoup the cost of distributing water to the Suburban Purchasers based on the methodology outlined in Article IV of the Suburban Water Rate Agreement (the Suburban Revenue Requirement). During fiscal years 2000 and 1999, the Suburban Revenue Requirement charged to such suburban customers was \$69,993 and \$64,537, respectively. Such amounts are subject to final review by the suburban customers, based on the Suburban Revenue Requirement calculation.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

Pursuant to Article V, Section 5.07 of the Suburban Water Rate Agreement, the City is required to recompute the Suburban Revenue Requirement after the close of each fiscal year based on the actual costs incurred in the delivery of water to the Suburban Purchasers. The difference between the suburban revenues earned during the year and the "actual" Suburban Revenue Requirement is recorded in a separate account (the Balancing Account) and represents the cumulative amount that is either owed to the Suburban Purchasers (if the suburban revenues exceed the Suburban Revenue Requirement) or owed to the City (if the Suburban Revenue Requirement exceeds the suburban revenues paid). In accordance with Article V of the Suburban Water Rate Agreement, the amount recorded in the Balancing Account shall earn interest at a rate equal to the average rate received by the City during the year on the invested pooled funds of the City Treasurer, and shall be taken into consideration in the determination of subsequent suburban water rates. Upon the expiration of the Suburban Water Rate Agreement, the remaining balance in the Balancing Account shall be settled between the City and the Suburban Purchasers. As of June 30, 2000 and 1999, the Suburban Purchasers owed the Department \$2,457 and \$5,807, respectively, under the terms of the Suburban Water Rate Agreement, and these amounts are reflected in the Suburban Water Rate Agreement receivables in the accompanying balance sheet.

(10) Employee Benefits

(a) Retirement Plan

Plan Description—The City has a single-employer defined benefit retirement plan (the Plan) which is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). The Plan covers substantially all full-time employees of the Department along with other employees of the City. The Plan provides basic service retirement, disability, and death benefits based on specified percentages of final average salary, and provides cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City and County Employees' Retirement System, 30 Van Ness Avenue, Suite 3000, San Francisco, CA 94102, or by calling (415) 487-7020.

Funding Policy—Contributions are made to the basic plan by both the Department and its employees. Employee contributions are mandatory. Employee contribution rates for 2000 and 1999 were between 7% and 8% as a percentage of covered payroll. The Department is required to contribute at an actuarially determined rate. No Department contributions were required for 2000 and 1999 as the actuarially determined contribution rate as a percentage of covered payroll was 0%. The Department's contributions to the Retirement System on behalf of its employees amounted to \$1,980, \$1,715 and \$1,579 for the years ended June 30, 2000, 1999, and 1998, respectively, which was equal to the required employee contributions for those years.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

(b) Health Care Benefits

Health care benefits of the Department's employees, retired employees, and surviving spouses are financed by beneficiaries and the City through the City and County of San Francisco Health Service System, an internal service fund. The Department's contributions covering current and retired employees, which amounted to approximately \$2,519 and \$2,318 in fiscal years 2000 and 1999, respectively, are determined by Charter provisions based on similar contributions made by the ten most populous counties in California. The Department's liability for both current employee and postretirement health care benefits is limited to its annual contribution.

(11) Related Parties

During 2000 and 1999, the Department delivered water without charge to certain City departments which amounted to approximately \$4,800 and \$4,700, respectively, based on metered usage and applicable water rates, which has been excluded from operating revenues in the accompanying financial statements.

Certain administrative costs of the Commission are allocated to the Department. For the years ended June 30, 2000 and 1999, the Commission allocated \$14,932 and \$14,927, respectively, in administrative costs to the Department, which are included in general and administrative expenses in the accompanying financial statements.

The Department purchases water from Hetch Hetchy. This amount, totaling \$19,037 for the years ended June 30, 2000 and 1999 has been included in the services provided by other departments' expense in the accompanying financial statements.

The Department purchases electricity from Hetch Hetchy. This amount, totaling \$3,874 and \$3,822 for the years ended June 30, 2000 and 1999, respectively, has been included in services provided by other departments in the accompanying financial statements.

A variety of City departments provides services such as engineering, purchasing, legal, data processing, telecommunication and human resources to the Department and charges amounts designed to recover those departments' costs. These charges totaling approximately \$5,300 and \$3,800 for the years ended June 30, 2000 and 1999, respectively, have been included in services provided by other departments in the accompanying financial statements.

The Department bills and collects sewer service charges on behalf of the San Francisco Clean Water Program.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(12) Risk Management

The Department is self-insured for general liabilities, property damage, and workers' compensation claims. The risk of loss is managed internally by setting aside assets for claim settlement and recording a liability representing an estimate of the cost of all outstanding claims and incurred but not reported claims. Claim liabilities are recorded when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount and, therefore, it is reasonably possible that claim liabilities could change in the future. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and legal factors. The liabilities have been actuarially determined. Changes in the reported liability for the years ended June 30 resulted from the following:

| | <u>2000</u> | <u>1999</u> |
|--|------------------|----------------|
| Beginning of year liability | \$ 6,499 | 8,189 |
| Current year claims and changes in estimates | 12,684 | 2,140 |
| Current year claims payments | <u>(2,106)</u> | <u>(3,830)</u> |
| End of year liability | \$ <u>17,077</u> | <u>6,499</u> |
| Damage and claims liability | \$ 13,380 | 3,444 |
| Accrued workers' compensation | <u>3,697</u> | <u>3,055</u> |
| | \$ <u>17,077</u> | <u>6,499</u> |

(13) Commitments and Litigation

(a) Commitments

As of June 30, 2000 and 1999, the Department has outstanding commitments with third parties of \$46,679 for various capital projects and other purchase agreements for materials and services.

(b) Grants

Grants that the Department receives are subject to audit and final acceptance by the granting agency. Current and prior year costs of such grants are subject to adjustment upon audit.

(c) Litigation

The Department is a defendant in various legal actions and claims that arise during the normal course of business, although the final disposition of those legal actions and claims is not determinable. However, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or results of operations of the Department.

SAN FRANCISCO WATER DEPARTMENT

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(d) Environmental Issue

In July 1999, the staff of the California Regional Water Quality Control Board issued a directive instructing the Commission to develop a remedial action plan that addresses environmental contamination located at certain real property owned by the Department. In response to the directive, the Commission developed a remedial action plan and is currently executing the plan. The Department has funded the initial year of the plan and will be requesting additional funding to complete its plan. Should the Department be subject to further regulatory direction regarding the remediation of the property, the cost of clean-up beyond that to which the Department has committed in its plan cannot be determined. No amount for additional clean-up beyond the Department's plan has been accrued in the accompanying financial statements.

(14) Subsequent Event

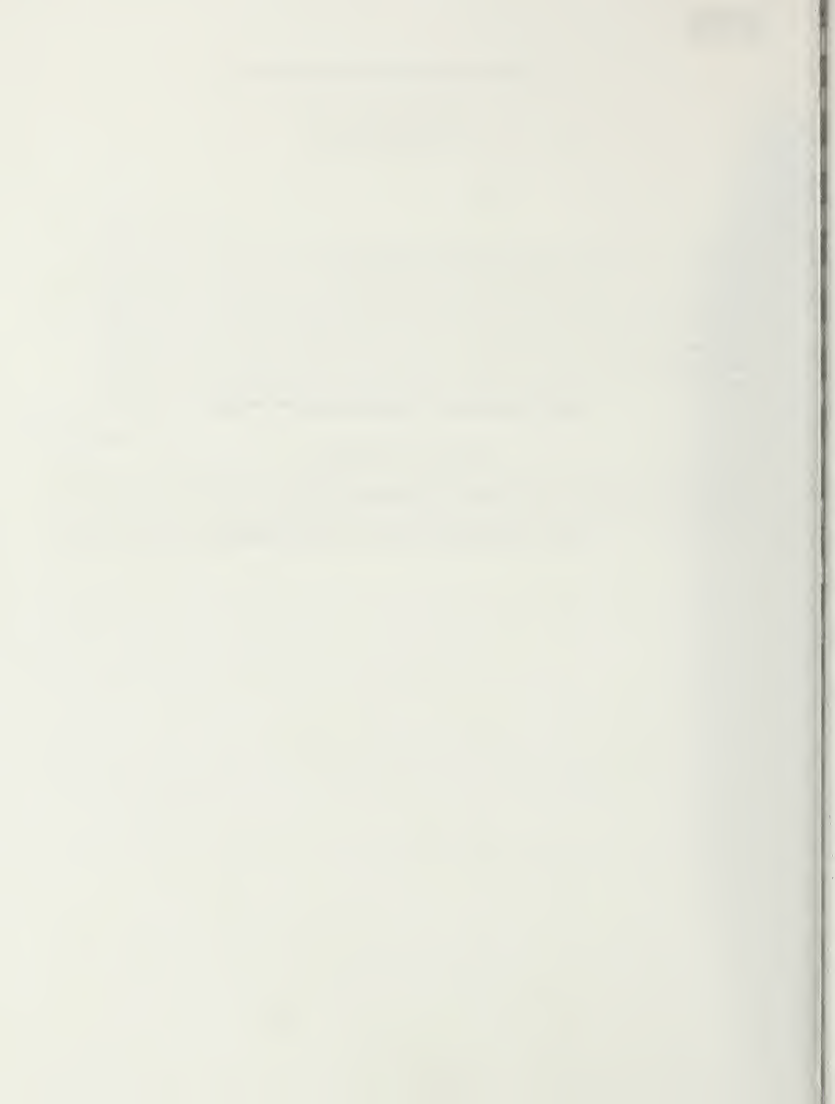
On October 10, 2000, the Public Utilities Commission authorized the expansion of up to \$250 million of commercial paper outstanding at any time. The commercial paper is sized to be adequate to fund the fiscal years 2000 and 2001 Water Enterprise capital appropriations. The expansion of the maximum amount of commercial paper that can be outstanding at any time was approved by the Board of Supervisors Finance Committee on October 25, 2000.

HETCH HETCHY WATER AND POWER

Financial Statements

June 30, 2000 and 1999

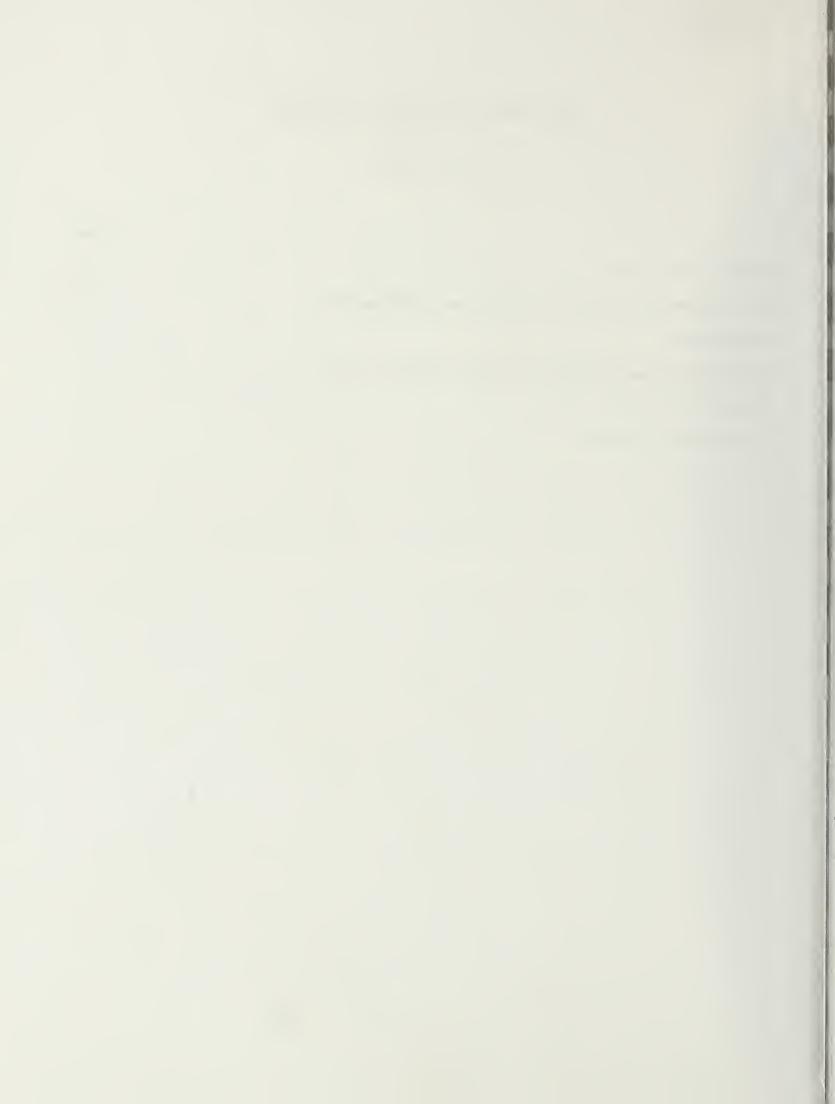
(With Independent Auditors' Report Thereon)



HETCH HETCHY WATER AND POWER

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Three Embarcadero Center
San Francisco, CA 94111

Independent Auditors' Report

Honorable Mayor and Board of Supervisors
City and County of San Francisco, California:

We have audited the accompanying financial statements of Hetch Hetchy Water and Power (Hetch Hetchy) of the City and County of San Francisco, California (the City), as of and for the years ended June 30, 2000 and 1999, as listed in the table of contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in note 1, the financial statements referred to above present only the financial activities of Hetch Hetchy and are not intended to present fairly the financial position of the City, and the results of its operations and the cash flows of its proprietary fund types in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Hetch Hetchy Water and Power of the City and County of San Francisco, California, as of June 30, 2000 and 1999, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

October 25, 2000



KPMG LLP, KPMG LLP, a U.S. limited liability partnership, is
a member of KPMG International, a Swiss association

HETCH HETCHY WATER AND POWER

Balance Sheets

June 30, 2000 and 1999
(in thousands)

| Assets | 2000 | 1999 |
|--|------------|---------|
| Current assets: | | |
| Deposits and investments with City Treasury | \$ 53,164 | 56,390 |
| Deposits and investments outside City Treasury | 10 | 14 |
| Receivables: | | |
| Charges for services | 8,338 | 8,769 |
| Due from the City and County of San Francisco | 4,132 | 4,745 |
| Interest and other | 1,346 | 1,295 |
| Total receivables | 13,816 | 14,809 |
| Inventories | 293 | 292 |
| Total current assets | 67,283 | 71,505 |
| Fixed assets, net | 207,276 | 203,240 |
| Total assets | \$ 274,559 | 274,745 |
| Liabilities and Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 7,822 | 11,044 |
| Accrued payroll | 833 | 661 |
| Accrued vacation and sick leave, current portion | 832 | 1,072 |
| Accrued workers' compensation, current portion | 247 | 223 |
| Damage and claims liability, current portion | 866 | 317 |
| Deposits, advances and other liabilities | 211 | 201 |
| Total current liabilities | 10,811 | 13,518 |
| Long-term liabilities: | | |
| Accrued vacation and sick leave | 864 | 1,203 |
| Accrued workers' compensation | 667 | 535 |
| Damage and claims liability | 4,957 | 2,013 |
| Other | 31 | 93 |
| Total long-term liabilities | 6,519 | 3,844 |
| Total liabilities | 17,330 | 17,362 |
| Equity: | | |
| Contributed capital | 6,717 | 1,661 |
| Retained earnings - unreserved | 250,512 | 255,722 |
| Total equity | 257,229 | 257,383 |
| Total liabilities and equity | \$ 274,559 | 274,745 |

See accompanying notes to financial statements.

HETCH HETCHY WATER AND POWER

Statements of Revenues, Expenses and Changes in Retained Earnings

Years ended June 30, 2000 and 1999
(in thousands)

| | <u>2000</u> | <u>1999</u> |
|---|-------------------|-----------------|
| Operating revenues: | | |
| Charges for services | \$ 109,584 | 105,707 |
| Rental income | 127 | 150 |
| Total operating revenues | <u>109,711</u> | <u>105,857</u> |
| Operating expenses: | | |
| Personal services | 12,029 | 11,608 |
| Contractual services | 3,702 | 3,393 |
| Purchased power | 30,468 | 20,271 |
| Materials and supplies | 1,531 | 1,460 |
| Depreciation and amortization | 8,638 | 8,383 |
| Services provided by other departments | 903 | 1,537 |
| General and administrative | 16,525 | 13,993 |
| Other | 5,800 | 2,145 |
| Total operating expenses | <u>79,596</u> | <u>62,790</u> |
| Operating income | <u>30,115</u> | <u>43,067</u> |
| Nonoperating revenues: | | |
| Federal grants | 1,456 | 244 |
| State/other grants | 103 | — |
| Interest and investment income | 2,296 | 2,173 |
| Other nonoperating revenues | 591 | 175 |
| Nonoperating revenues | <u>4,446</u> | <u>2,592</u> |
| Income before operating transfers | <u>34,561</u> | <u>45,659</u> |
| Operating transfers to the City and County of San Francisco | <u>(39,850)</u> | <u>(42,703)</u> |
| Net (loss) income | (5,289) | 2,956 |
| Depreciation expenses against contributed capital | 79 | — |
| Retained earnings at beginning of year | <u>255,722</u> | <u>252,766</u> |
| Retained earnings at end of year | <u>\$ 250,512</u> | <u>255,722</u> |

See accompanying notes to financial statements.

HETCH HETCHY WATER AND POWER

Statements of Cash Flows

Years ended June 30, 2000 and 1999
(in thousands)

| | 2000 | 1999 |
|---|-----------|----------|
| Cash flows from operating activities: | | |
| Cash received from customers, including cash deposits | \$ 46,843 | 44,332 |
| Cash received from quasi-external transactions | 62,741 | 60,278 |
| Cash received from tenants for rent | 127 | 150 |
| Cash paid to employees for services | (11,964) | (10,826) |
| Cash paid to suppliers for goods and services | (42,990) | (26,820) |
| Cash paid to other governments | (4,485) | (4,996) |
| Cash paid for fees, licenses and permits | (2,173) | (1,810) |
| Cash paid for judgements and claims | (350) | (175) |
| Cash paid for quasi-external transactions | (7,649) | (6,498) |
| Net cash provided by operating activities | 40,100 | 53,635 |
| Cash flows from noncapital financing activities: | | |
| Operating grants | 1,224 | 178 |
| Operating transfers out | (39,850) | (42,703) |
| Net cash used in noncapital financing activities | (38,626) | (42,525) |
| Cash flows from capital and related financing activities: | | |
| Acquisition and construction of capital assets | (7,536) | (6,820) |
| Payment of capital lease obligations | (55) | (55) |
| Net cash used in capital and related financing activities | (7,591) | (6,875) |
| Cash flows from investing activities: | | |
| Interest income received | 2,706 | 2,597 |
| Other investing activities | 591 | 175 |
| Net cash provided by investing activities | 3,297 | 2,772 |
| (Decrease) increase in cash and cash equivalents | (2,820) | 7,007 |
| Cash and cash equivalents: | | |
| Beginning of year | 56,835 | 49,828 |
| End of year | \$ 54,015 | 56,835 |

HETCH HETCHY WATER AND POWER

Statements of Cash Flows

Years ended June 30, 2000 and 1999
(in thousands)

| | <u>2000</u> | <u>1999</u> |
|---|------------------|---------------|
| Reconciliation of operating income to net cash provided by operating activities: | | |
| Operating income | \$ 30,115 | 43,067 |
| Adjustments to reconcile operating income to net cash provided by operating activities: | | |
| Depreciation and amortization | 8,638 | 8,383 |
| Changes in assets and liabilities: | | |
| Receivables: | | |
| Charges for services | 431 | (1,014) |
| Due from City and County of San Francisco | 613 | (3,001) |
| Other | 284 | 1,252 |
| Inventories | (1) | (22) |
| Accounts payable | (3,222) | 2,441 |
| Accrued payroll | 172 | 80 |
| Accrued vacation and sick leave | (579) | 142 |
| Accrued workers' compensation | 156 | 305 |
| Damage and claims liability | 3,493 | 2,085 |
| Deposits, advances and other liabilities | — | (83) |
| Net cash provided by operating activities | <u>\$ 40,100</u> | <u>53,635</u> |
| Reconciliation of cash and cash equivalents to the balance sheet: | | |
| Deposits and investments with City Treasury | \$ 53,164 | 56,390 |
| Deposits and investments outside City Treasury | <u>10</u> | <u>14</u> |
| Total deposits and investments | 53,174 | 56,404 |
| Add unrealized loss on investments | <u>841</u> | <u>431</u> |
| Cash and cash equivalents at end of year on statement of cash flows | <u>\$ 54,015</u> | <u>56,835</u> |

See accompanying notes to financial statements.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(1) The Financial Reporting Entity

Hetch Hetchy Water and Power (Hetch Hetchy) was established as a result of the Raker Act of 1913, which granted water and power resources rights-of-way on the Tuolumne River in Yosemite National Park to the City of San Francisco. Hetch Hetchy is engaged in the collection and conveyance of approximately 85% of San Francisco's water supply and in the generation and transmission of electricity from that resource. Approximately one-third of the electricity is used by the San Francisco's municipal customers (e.g., the San Francisco Municipal Railway, the Recreation and Parks Department, the Port of San Francisco, San Francisco County hospitals, street lighting, Moscone Center, and the water and sewer utilities). The balance of the power generated is sold to other publicly owned utilities, such as the Modesto and Turlock Irrigation Districts. Hetch Hetchy consists of a system of reservoirs, hydroelectric power plants, aqueducts, pipelines, and transmission lines. This system carries water and power more than 165 miles from the Sierra Nevada to customers in the City of San Francisco and portions of the surrounding San Francisco Bay Area.

The San Francisco Public Utilities Commission (the Commission), established in 1932, is responsible for providing operational oversight of the public utility enterprises of the City and County of San Francisco (the City), which include Hetch Hetchy along with the City's water and sewer utilities (e.g., the San Francisco Water Department and the San Francisco Clean Water Program). The Commission consists of five members appointed by the Mayor who are responsible for determining such matters as the rates and charges for services, approval of contracts, and organizational policy. The Commission is a department of the City and, as such, the financial operations of Hetch Hetchy, the San Francisco Water Department, and the San Francisco Clean Water Program are included in the Comprehensive Annual Financial Report of the City as enterprise funds. These financial statements present only the financial operations of the Hetch Hetchy and are not intended to present the financial position of the City, the results of its operations and the cash flows of its proprietary fund types.

(2) Significant Accounting Policies

(a) *Basis of Accounting—Fund Accounting*

The accounts of Hetch Hetchy are organized on the basis of a proprietary fund type, specifically an enterprise fund. The operations of this fund are accounted for with a separate set of self-balancing accounts that comprise Hetch Hetchy's assets, liabilities, fund equity, revenues, and expenses. Enterprise Funds account for operations (i) that are financed and operated in a manner similar to private business enterprises where the intent of the Commission is that Hetch Hetchy's costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (ii) where the Commission has decided that periodic determination of revenues earned, expenses incurred, and net income or loss of Hetch Hetchy is appropriate for capital maintenance, public policy, management control, accountability, or other purpose.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

(b) Measurement Focus

The financial activities of Hetch Hetchy are accounted for on a flow of economic resources measurement focus, using the accrual basis of accounting. Under this method, all assets and liabilities associated with operations are included on the balance sheet; revenues are recorded when earned, and expenses are recorded when liabilities are incurred.

Hetch Hetchy does not apply Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989. Hetch Hetchy applies all applicable Governmental Accounting Standards Board (GASB) pronouncements, as well as statements and interpretations of FASB, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedures issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

(c) Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid investments, including restricted assets, with an original purchased maturity of three months or less.

(d) Investments

Investments are stated at fair value based on quoted market prices. Changes in fair value are recognized as investment income.

Money market funds that have a remaining maturity at the time of purchase of one year or less are carried at amortized cost.

(e) Inventory

Inventory primarily consists of construction materials and maintenance supplies and is valued at average cost. Inventory is expensed as it is consumed.

(f) Fixed Assets

Fixed assets are stated at cost. Depreciation and amortization are computed by using the straight-line method based on the estimated useful lives of the related assets, which range from 3 to 75 years for equipment and 3 to 100 years for buildings, structures, and improvements. No depreciation or amortization is recorded in the year of acquisition, and a full year's depreciation or amortization is recorded in the year of disposal.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(g) Construction in Progress

The cost of acquisition and construction of major plant and equipment is recorded as construction in progress. As facilities are accepted by Hetch Hetchy and become operative, they are transferred to the plant and equipment accounts, and depreciated in accordance with Hetch Hetchy's depreciation policies. Costs of construction projects that are discontinued are recorded as expense in the year in which the decision is made to discontinue such projects.

(h) Accrued Vacation and Sick Leave

Accrued vacation pay, which may be accumulated up to ten weeks per employee, is charged to expense as earned. Unused sick leave accumulated through December 6, 1978 is vested and payable upon termination of employment by retirement, death, or disability caused by industrial accident. Sick leave earned subsequent to that date is nonvesting and may be accumulated up to six months per employee.

(i) Workers' Compensation

Hetch Hetchy is self-insured for workers' compensation claims and accrues the estimated cost of those claims, including the estimated cost of incurred but not reported claims.

(j) Damage and Claims Liability

Hetch Hetchy is self-insured for general liability and property damage claims. The liability represents an estimate of the cost of all outstanding claims, including adverse loss development, and estimated incurred but not reported claims.

(k) Income Taxes

As a government agency, Hetch Hetchy is exempt from both federal income taxes and California state franchise taxes.

(l) Revenue Recognition

Revenues from water and power services furnished to consumers are recorded in the financial statements in the period that meters are read.

(m) Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(n) *Reclassifications*

Certain reclassifications have been made to the 1999 financial statements to conform to the 2000 presentation. These reclassifications did not change total assets, liabilities, equity, or net income.

(3) **Cash and Investments**

The captions on the balance sheet related to cash and investments as of June 30 2000 and 1999 are as follows:

| | <u>2000</u> | <u>1999</u> |
|--|------------------|---------------|
| Deposits and investments with City Treasury | \$ 53,164 | 56,390 |
| Deposits and investments outside City Treasury | <u>10</u> | <u>14</u> |
| | \$ <u>53,174</u> | <u>56,404</u> |

Investments

Hetch Hetchy's deposits and investments with the City Treasury are invested pursuant to investment policy guidelines established by the City Treasurer. The objectives of the policy guidelines are, in order of priority, preservation of capital, liquidity, and yield. The policy addresses soundness of financial institutions in which the City will deposit funds, types of investment instruments as permitted by the California Government Code, and the percentage of the portfolio which may be invested in certain instruments with longer terms to maturity. The City's Comprehensive Annual Financial Report categorizes the level of custodial risk associated with its pooled cash and investments, which includes \$53,164 and \$56,390 of Hetch Hetchy's total deposits and investments as of June 30, 2000 and 1999, respectively. The City Treasurer allocates monthly income from the investment of pooled cash in proportion to Hetch Hetchy's end-of-month balances.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(4) Fixed Assets

A summary of changes in fixed assets follows:

| | Balance June 30, 1999 | Additions | Deletions and transfers | Balance June 30, 2000 |
|-----------------------------|----------------------------------|------------------|------------------------------------|----------------------------------|
| Land | \$ 4,215 | — | — | 4,215 |
| Facilities and improvements | 375,390 | 7,384 | — | 382,774 |
| Machinery and equipment | 26,614 | 6,790 | (59) | 33,345 |
| Accumulated depreciation | (212,943) | (8,683) | 46 | (221,580) |
| | <u>193,276</u> | <u>5,491</u> | <u>(13)</u> | <u>198,754</u> |
| Construction-in-progress | 9,964 | — | (1,442) | 8,522 |
| Total | <u>\$ 203,240</u> | <u>5,491</u> | <u>(1,455)</u> | <u>207,276</u> |

(5) Employee Benefits

(a) Retirement Plan

Plan Description—The City has a single-employer defined benefit retirement plan (the Plan) which is administered by the San Francisco City and County Employees' Retirement System (the Retirement System). The Plan covers substantially all full-time employees of Hetch Hetchy along with other employees of the City. The Plan provides basic service retirement, disability and death benefits based on specified percentages of final average salary, and provides cost-of-living adjustments after retirement. The Plan also provides pension continuation benefits to qualified survivors. The San Francisco City and County Charter and Administrative Code is the authority which establishes and amends the benefit provisions and employer obligations of the Plan. The Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained by writing to the San Francisco City and County Employees' Retirement System, 30 Van Ness Avenue, Suite 3000, San Francisco, CA 94102, or by calling (415) 487-7020.

Funding Policy—Contributions are made to the basic plan by both Hetch Hetchy and its employees. Employee contributions are mandatory. Employee contribution rates for 2000 and 1999 were between 7% and 8% as a percentage of covered payroll. Hetch Hetchy is required to contribute at an actuarially determined rate. No Hetch Hetchy contributions were required for 2000 and 1999 as the actuarially determined contribution rate as a percentage of covered payroll was 0%. Hetch Hetchy's contributions to the Retirement System on behalf of its employees amounted to \$773, \$611 and \$540 for the years ended June 30, 2000, 1999 and 1998, respectively, which was equal to the required employee contributions for those years.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(b) Health Care Benefits

Health care benefits of Hetch Hetchy's employees, retired employees, and surviving spouses are financed by beneficiaries and the City through the City and County of San Francisco Health Service System, an internal service fund. Hetch Hetchy's contributions covering current and retired employees, which amounted to approximately \$1,005 and \$880 in fiscal years 2000 and 1999, respectively, are determined by Charter provisions based on similar contributions made by the ten most populous counties in California. Hetch Hetchy's liability for both current employee and postretirement health care benefits is limited to its annual contribution.

(6) Related Parties

Included in 2000 and 1999 operating revenues are sales of power to departments within the City of \$43,704 and \$41,241, respectively.

Income from Hetch Hetchy is available for certain operations of the City. During the years ended June 30, 2000 and 1999, Hetch Hetchy transferred \$39,850 and \$42,703, respectively, to the General Fund.

A variety of City departments provide services such as engineering, purchasing, legal, data processing, telecommunication and human resources to Hetch Hetchy and charge amounts designed to recover those departments' costs. These charges totaling approximately \$1,312 and \$1,200 for the years ended June 30, 2000 and 1999, respectively, have been included in services provided by other departments in the accompanying financial statements.

Certain administrative costs of the Commission are allocated to Hetch Hetchy. For the years ended June 30, 2000 and 1999, the Commission allocated \$5,901 and \$4,728, respectively, in administrative costs to Hetch Hetchy which are included in general and administrative expenses in the accompanying financial statements.

The San Francisco Water Department purchases water from Hetch Hetchy. This amount, totaling \$19,037 for the years ended June 30, 2000 and 1999, has been included in operating revenues in the accompanying financial statements.

Hetch Hetchy serves as an intermediary agency between the Pacific Gas & Electric Company (PG&E) and all City departments for the design and construction of various electrical components and other related systems needed to deliver electricity. As an intermediary agency, Hetch Hetchy is responsible for the payment of all invoices to PG&E and its subcontractors. The total cost of the facilities including certain labor and administration costs incurred by Hetch Hetchy are charged back to the related departments. As of June 30, 2000 and 1999, various City departments were indebted to Hetch Hetchy for unrecovered construction costs of approximately \$4.1 million and \$4.7 million, respectively, and these amounts are included in the amount due from the City and County of San Francisco in the accompanying financial statements.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(7) Contributed Capital

The San Francisco International Airport (the Airport) is currently undergoing a major expansion project that will substantially increase future demand for electrical power. In December 1994, the City entered into two special facilities agreements (the Agreements) with PG&E to increase the capacity of existing PG&E equipment and systems at the Airport and Millbrae Substations to accommodate the Airport's projected increased load. Subsequent to seeking approval from the Federal Energy Regulatory Commission (FERC), staff from the Airport and Hetch Hetchy developed an alternate project configuration. Under the alternate configuration, PG&E would construct a new City-owned substation to be located on Airport property and would replace existing PG&E equipment at the current Airport Substation with City-owned equipment. Under the conditions of the alternate project configuration, PG&E would convey to the City all rights, title and interests that PG&E has with regards to the new facilities upon their completion. In accordance with standard utility practice, the cost of these facilities was funded entirely by the Airport, and upon completion of each project phase, Hetch Hetchy would receive title to these assets from PG&E on behalf of the City. In addition, as the City's electric utility, Hetch Hetchy would assume responsibility for the operations, maintenance, repair and replacement of the facilities following their initial year of operation.

In July 1999, PG&E conveyed title to facilities and associated equipment to Hetch Hetchy pursuant to the alternate project configuration. In fiscal 2000 of the total facilities and equipment that was contributed to Hetch Hetchy amounted to approximately \$5.1 million. Contributed facilities and equipment total \$6.8 million as of June 30, 2000.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

(8) Risk Management

Hetch Hetchy is self-insured for general liabilities, property damage, and workers' compensation claims. The risk of loss is managed internally by setting aside assets for claim settlement and recording a liability representing an estimate of the cost of all outstanding claims and incurred but not reported claims. Claim liabilities are recorded when it is probable that a loss has occurred and the amount of loss can be reasonably estimated. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount and, therefore, it is reasonably possible that claim liabilities could change in the future. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and legal factors. The liabilities have been actuarially determined. Changes in the reported liability for the years ended June 30, 2000 and 1999 resulted from the following:

| | <u>2000</u> | <u>1999</u> |
|--|---------------------|---------------------|
| Beginning of year liability | \$ 3,088 | 698 |
| Current year claims and changes in estimates | 3,999 | 2,565 |
| Current year claims payments | <u>(350)</u> | <u>(175)</u> |
| End of year liability | <u>6,737</u> | <u>3,088</u> |
| Damage and claims liability | 5,823 | 2,330 |
| Accrued workers' compensation | <u>\$ 914</u> | <u>758</u> |
| | <u><u>6,737</u></u> | <u><u>3,088</u></u> |

(9) Deregulation of the California Electric Industry

Effective April 1, 1998, the California electric market fundamentally changed into a competitive market which permitted customers of investor-owned utilities (IOU) to be eligible for direct access. In other words, an electric utility customer can freely choose the provider of their electric service. The enabling legislation, Assembly Bill 1890 (AB 1890), applies primarily to investor-owned utilities, but strongly encourages public agency-owned utilities to elect to participate in the competitive framework of the California electric market.

AB 1890 also called for the creation of a power exchange (PX) which is responsible for managing the dispatch of IOU energy generation. Additionally, AB 1890 provided for creation of the Independent System Operator (ISO) which is responsible for managing the transmission grid in California. AB 1890 further provided electric utilities with a basis for recovery of "stranded costs" through the implementation of an accelerated nonbypassable competition transition charge (CTC), subject to certain restrictions. These stranded costs consist primarily of (a) debt service payments to bondholders for bond financed generation-related assets, and (b) obligations (including power purchase contracts) on which entities are legally obligated to pay and which cannot be mitigated because of contract restrictions, and/or competitive market conditions.

HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999

(dollars in thousands)

The deregulation of the electric industry has created a substantially changed market for electricity. The regulated industry operating market environment is being replaced by competition, namely direct access. In anticipation of this restructured market, Hetch Hetchy is developing a strategic plan that will guide its electric utility's transition efforts into the new environment.

(10) Commitments and Litigation

(a) *Commitments*

The Commission has contracted with PG&E to provide transmission capacity on PG&E's system where needed to deliver Hetch Hetchy's power to its customers. In addition, the PG&E agreement provides backup power and other support services to Hetch Hetchy. The PG&E agreement allows PG&E to review past billings paid by Hetch Hetchy and to retroactively adjust these payments to actual backup power, transmission and other charges as finally determined by PG&E. During fiscal years 2000 and 1999, Hetch Hetchy purchased \$14,368 and \$13,365, respectively, of transmission services, backup power and other support services from PG&E under the terms of the agreement.

To meet certain requirements of the Don Pedro Reservoir operating license, the City entered into an agreement with the Modesto and Turlock Irrigation Districts (the Districts) in which the Districts would be responsible for an increase in water flow releases from the reservoir in exchange for annual payments of \$3,500 from the City. The payments are to be made for the duration of the license, but may be terminated with one year's prior written notice after 2001. The City and the Districts have also agreed to monitor the fisheries in the lower Tuolumne River for the duration of the license. A maximum monitoring expense of \$1,400 is to be shared between the City and the Districts over the term of the license. The City's share of the monitoring costs is 52% while the Districts are responsible for 48% of the costs.

As of June 30, 2000 and 1999, Hetch Hetchy has outstanding commitments with third parties of \$5,289 for various capital projects and other purchase agreements for materials and services.

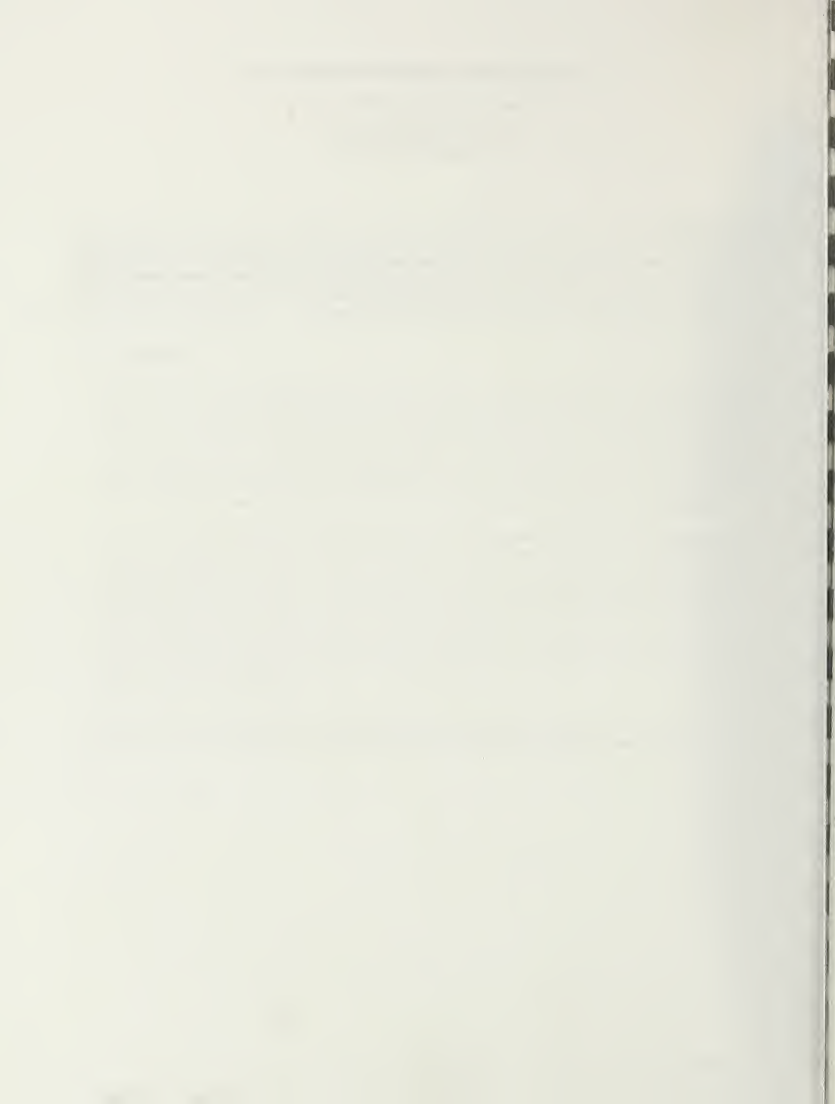
HETCH HETCHY WATER AND POWER

Notes to Financial Statements

June 30, 2000 and 1999
(dollars in thousands)

(b) Litigation

Hetch Hetchy is a defendant in various legal actions and claims that arise during the normal course of business. The final disposition of these legal actions and claims is not determinable; however, in the opinion of management, the outcome of any litigation of these matters will not have a material effect on the financial position or results of operations of Hetch Hetchy.





Front Cover Photo: Pulgas Water Temple, built in 1934, commemorates the terminus of the long journey that water makes 167 miles from Yosemite National Park to the Crystal Springs Reservoir.

Back Cover Photo: Terra cotta final at the crown of the Sunol Temple was designed by Willis Polk and manufactured by Gladding Mc Bean in 1910.



Fiscal Year 2000 - 2001 Annual Report

SAN FRANCISCO PUBLIC UTILITIES COMMISSION
CITY AND COUNTY OF SAN FRANCISCO

HETCH HETCHY WATER AND POWER
SAN FRANCISCO WATER ENTERPRISE
DOCUMENTS DEPARTMENT CLEAN WATER ENTERPRISE



The San Francisco Public Utilities Commission (SFPUC) oversees three of the City and County of San Francisco's (the City) municipal utilities:

- Hetch Hetchy Water and Power Enterprise consists of water supply and power generation facilities in the Sierra Nevada;

- The San Francisco Water Enterprise consists of a treatment and distribution system which delivers drinking water to more than 2.4 million customers in the San Francisco Bay Area;

- The Clean Water Enterprise treatment and disposal system collects and treats sewage and storm water flows within the City.

Each of the three utilities represents a separate enterprise within the SFPUC, which operates as a department of the City. The Mayor of San Francisco appoints a five-member Commission each for four-year terms to govern the SFPUC. The Commission appoints the General Manager who serves as the chief administrative officer and is responsible for the SFPUC's day-to-day operations. The General Manager provides overall direction and leadership, appoints senior staff to manage the three Enterprises, and oversees the activities of the SFPUC.

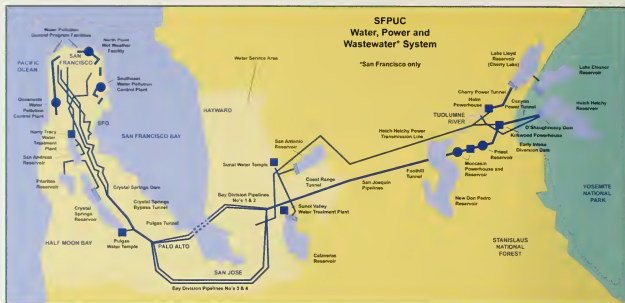


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Willie L. Brown, Jr., Mayor
City & County of San Francisco
San Francisco Public Utilities Commission

SFPUC Commissioners

Ann Moller Caen, President
E. Dennis Normandy, Vice President
Frank L. Cook, Commissioner
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SFPUC Commissioners Bhatt, Caen, Normandy, Cook, and Chen.

A Message from....Pat Martel, General Manager

The Honorable Mayor Willie L. Brown, Jr.
City & County of San Francisco Board of Supervisors
San Francisco Public Utilities Commission

RE: Fiscal Year 2001 Annual Report

It is with great pleasure that I present the Fiscal Year 2001 Annual Report of the San Francisco Public Utilities Commission (SFPUC). Fiscal Year 2001 was fiscally and organizationally challenging for the SFPUC. The challenges faced by the SFPUC resulted from the California energy crisis, the complexity of developing a comprehensive capital improvement plan, the dawning of an economic recession, and various operational as well as organizational issues. Nonetheless, the SFPUC remained steadfast in its commitment to provide customers with high quality and reliable water and uninterrupted power supplies, as well as first-rate customer service. Maintaining requisite fiscal prudence, especially in light of Proposition H, has made such endeavors even more difficult.

The California power crisis and the ensuing increase in power price volatility significantly impacted Hetch Hetchy Enterprise's operating results for the fiscal year. It also portends considerable financial challenge in dealing with Hetchy's future years' drought risk exposures. Hetch Hetchy's cost of purchased power for the fiscal year increased by \$24.3 million over the prior year. In response, the SFPUC worked closely with the California Independent System Operator (ISO), the Mayor's Office, and customers with significant load to implement voluntary energy curtailment and conservation programs. In addition, Hetch Hetchy sought to diversify its hydro-based power portfolio with the acquisition of power contracts. Other initiatives, including resource development and transmission line extensions, are currently under way to ensure power supply reliability, a diversified power portfolio, and sustained efforts to mitigate drought and financial risk exposures going forward.

Although the Water Enterprise was constrained by Proposition H, it ended the fiscal year with a net asset increase of \$129 million, which represents a significant increase from the prior fiscal year. This superior performance is attributed to a combination of a slight increase in operating revenues, and approximately \$126 million from the sale of property owned by the Water Enterprise. These funds are being plowed back into capital maintenance and other system improvement projects. In addition, the SFPUC is continuing to make progress toward the execution of the water quality and seismic improvement projects funded with Proposition A and B Bonds. The Alameda Watershed Management Plan designed to protect water quality in local reservoirs and environmental values on the watershed was adopted during the fiscal year. The Sunol Water Temple renovation was also completed and opened to the public in fiscal year 2001.

The Clean Water Enterprise provided outstanding service to San Francisco customers and received several distinguished awards for regulatory compliance excellence during the fiscal year. However, the SFPUC's inability to raise rates pursuant to Proposition H in the face of rising treatment and energy costs, resulted in an approximately 21% decline in the profitability of the Clean Water Enterprise compared to the prior fiscal year.

The SFPUC is continuing efforts to develop a comprehensive Capital Improvement Program (CIP) to refurbish the system's aging infrastructure, and provide adequate future capacity, sustained quality and reliable customer service. Also of note this past fiscal year, the SFPUC successfully introduced the online bill account maintenance service and efforts are underway to implement a one-stop customer service center.

Looking ahead, many challenges remain. As the new General Manager, my resolve is unwavering, as the entire SFPUC staff and I deal with these challenges in the coming months. We will seek the input of our valued stakeholders as we proceed to execute our critical mandates of delivering high quality, reliable water and power. As we move forward, our goal of superior customer service will remain the vanguard of our operations.



Patricia Martel
General Manager

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Hetchy Facts

- 660,000 acre feet of water storage facilities
- 4 hydroelectric power plants with combined peak capacity of 400 megawatts
- 650 square miles of forested watershed
- More than 160 miles of aqueducts, pipelines, high-voltage transmission systems, and rights-of-way
- Supplies average of 220 million gallons of water per day (MGD)
- 85% of San Francisco drinking water supply
- 15% of San Francisco electricity supply

Current Year Hetchy Facts

- 25 inches of precipitation
- 360,000 acre-feet snowmelt inflow at Hetch Hetchy Reservoir from April to July - 60% of historic average
- 191,000 acre-feet spring runoff at Lakes Lloyd and Eleanor from April to July - 61% of historic average
- 1.7 billion kilowatt hours total generation

Hetch Hetchy Water and Power

Hetch Hetchy Water and Power (Hetch Hetchy) is a water and power enterprise, which provides reliable water and electricity to its customers while safeguarding the resources and assets entrusted to its care. Under pre-1914 water rights, Hetch Hetchy collects water in several reservoirs on federal lands pursuant to rights-of-way granted to the City through federal legislation in 1913 (the Raker Act). The purity of Hetch Hetchy water makes filtering unnecessary. The Raker Act required Hetch Hetchy to develop power generation in order to maximize the beneficial use of the water.

Hydroelectric power from Hetch Hetchy provides electricity to City facilities (e.g., City Hall, the Municipal Railway, Moscone Center, the Port, the Airport, Department of Recreation and Parks, City hospitals, City street lighting, water and sewer utilities, etc.). Power is also sold to a limited number of retail customers in San Francisco and other public agencies and municipalities on a wholesale basis. Hetch Hetchy's wholesale power customers include the Modesto and Turlock Irrigation Districts, which have priority rights under the Raker Act for municipal and agricultural uses within the boundaries of their respective service territories.

FY2000-01 Highlights

- California Power Crisis - focused on protecting the City from adverse impact, which took several dimensions, including: management of power outages, establishment of rotating blackout protocols and an energy curtailment program, and securing a fixed price, forward contract to purchase electricity from a third party over the next five years.
- Electric Utility Deregulation - worked with the California Independent System Operator (ISO) to enhance transmission channels and distribution of power throughout the City.
- Energy Resource Diversification - continued efforts to develop a diversified portfolio of energy resources to reduce hydrology risk.



Financial Analysis

Net Assets decreased by \$11.4 million or 4.4% in fiscal year 2001 mainly due to unfavorable operations.

Operating revenues increased by \$11.3 million or 10.3% to \$121 million primarily due to the increase in charges for services resulting from the increase in sales and rate increase to other City departments, power sales to Western System Power Pool, receipts from Pacific Gas & Electric Company for the Demand Reduction Program, and receipts from the Independent System Operator settlement.

Operating expenses increased by \$27.4 million or 34.4% to \$107 million, primarily due to the increase in the cost of purchased power, which was a direct result of the acute acceleration of electricity prices during the fiscal year.

Capital contributions represent the transfer of assets to Hetch Hetchy from the San Francisco International Airport (the Airport) as a result of the phased completion of a power substation located at Airport property.

Transfers to CCSF represent amounts provided to the City to finance the General Fund. As the amount of the transfer is contingent upon the operational performance of Hetch Hetchy, the decrease in the transfer from the prior fiscal year is due to the decrease in Hetch Hetchy operating income.

These results are based on the enterprise's audited financial statements.

Summary of Financial Operations (000s)

Comparative Net Assets

| | 2001 | 2000 |
|--|----------------|----------------|
| Current and other assets | \$59,124 | \$67,283 |
| Capital assets, net | 205,071 | 207,276 |
| Total assets | 264,195 | 274,559 |
| Current liabilities | 12,023 | 10,811 |
| Long-term liabilities | 6,372 | 6,519 |
| Total liabilities | 18,395 | 17,330 |
| Net Assets: | | |
| Invested in capital assets, net related debt | 205,071 | 207,276 |
| Unrestricted | 40,729 | 49,953 |
| Total net assets | 245,800 | 257,229 |

Changes in Net Assets

| | | |
|--|-----------------|-----------------|
| Operating revenues: | | |
| Charges for services | \$ 120,863 | \$ 109,584 |
| Rental income | 137 | 127 |
| Total operating revenues | 121,000 | 109,711 |
| Operating expenses: | | |
| Personal services | 14,243 | 12,029 |
| Materials and supplies | 1,293 | 1,531 |
| Purchased power | 44,237 | 19,982 |
| Transmission costs | 10,666 | 10,486 |
| General and administrative | 11,711 | 16,525 |
| Other operating expenses | 24,850 | 19,043 |
| Total operating expenses | 107,000 | 79,596 |
| Operating income | 14,000 | 30,115 |
| Nonoperating revenues, net | 4,151 | 4,446 |
| Capital contributions | 270 | 5,135 |
| Transfers to CCSF | (29,850) | (39,850) |
| Change in net assets | (11,429) | (154) |
| Net assets at beginning of year | 257,229 | 257,383 |
| Net assets at end of year | 245,800 | 257,229 |

Water Facts

Regional Water

- 40,000 acre watershed in Alameda County
- 23,000 acre watershed on the Peninsula
- Harry Tracy Treatment Plant: 143 MGD
- Sunol Treatment Plant: 118 MGD
- Provides 15% of water supply from Alameda and Peninsula watersheds

Local Water

- 17 pump stations
- 12 reservoirs
- 10 disinfection stations
- 9 water storage tanks
- 8 water pressure reducing stations
- 1250 miles of water mains within San Francisco, Yerba Buena Island, Treasure Island and Hunter's Point

Current Year Water Facts

- Accounts serviced: 169,735
- Consumption: 255.3 MGD

Water Supply & Treatment

- Harry Tracy Treatment Plant average treatment: 39 MGD
- Sunol Treatment Plant average treatment: 55 MGD
- Replaced 600 feet of the San Antonio Pipeline

City Distribution Division

- Responded to 136 two (or greater) alarm fires
- 246 water main connections
- 201 new service installations
- 153 water main break repairs
- 5,196 meter repairs/replacements

San Francisco Water Enterprise

The Water Enterprise consists of two divisions, the Water Supply & Treatment Division and the City Distribution Division.

Water Supply and Treatment Division (WST) is responsible for the water (from Hetch Hetchy) supplies to 1.6 million customers in Alameda, Santa Clara and San Mateo counties, and 800,000 in the City and County of San Francisco. Its mission is to operate as an effective, reliable regional water supplier, while managing resources in an environmentally sound manner.

City Distribution Division (CDD) is responsible for the transmission, storage and delivery of water to San Francisco's residential and commercial customers. CDD also provides a range of services, which include 24 hour-a-day on-call emergency response and technical assistance to other utilities. The division maintains, repairs, and upgrades water mains; provides assistance to customers' water concerns (i.e., underground leak detection and repair); and oversees work performed by outside utilities, developers, and contractors. It provides landscape maintenance for 984 acres of division lands, including rights-of-way, reservoirs, open space, and parks.

FY2000-01 Highlights

- Completed Sunol Temple renovations; now open to the public.
- Began installation of control valves on Bay Division pipelines.
- Initiated construction of the Tesla Portal Emergency Chlorine Station.
- Designed 12 water main and feeder replacement projects.



Financial Analysis

Net assets increased by \$129 million mainly due to a gain on the sale of property (500 acres of land) in Pleasanton, Alameda County during the fiscal year.

Operating revenues increased by \$5.7 million or 3.9% to \$149.9 million primarily due to the increase in charges for services of \$3.2 million and custom work (reported as other revenue) of \$1.9 million. Custom work represents special orders made of the Water Enterprise related to newly constructed facilities within the City.

Operating expenses increased by \$2.6 million or 1.8% to \$152 million, mainly due to the net impact of a decrease in day-to-day operating expenses and the recognition of an environmental clean-up expense. This expense stems from a long-term liability of \$22.8 million related to the cleanup of environmental contamination located at certain real property owned by the Water Enterprise.

The prior period adjustment represents the restatement of prior year revenues. While revenues for fiscal year 2000 related to a 12-month period, it did not correspond to revenues earned from July 1999 to June 2000, but rather June 1999 to May 2000. In addition, revenue earned but unbilled in the last month of each fiscal year was not accrued during the year, but recorded in the subsequent fiscal year. This adjustment accrues for revenues earned but unbilled and captures revenues related to the correct fiscal period.

These results are based on the enterprise's audited financial statements.

Summary of Financial Operations (000s)

Comparative Net Assets

| | 2001 | 2000 |
|--|----------------|----------------|
| Current and other assets | \$301,159 | \$164,183 |
| Capital assets, net | 529,887 | 461,798 |
| Total assets | 831,046 | 625,981 |
| Current liabilities | 118,228 | 57,995 |
| Long-term liabilities | 259,001 | 243,192 |
| Total liabilities | 377,229 | 301,187 |
| Net Assets: | | |
| Invested in capital assets, net related debt | 237,035 | 227,678 |
| Restricted | 40,941 | 52,770 |
| Unrestricted | 175,841 | 44,346 |
| Total net assets | 453,817 | 324,794 |

Changes in Net Assets

| | | |
|---|----------------|----------------|
| Operating revenues: | | |
| Charges for services | \$135,779 | \$132,551 |
| Rents and concessions | 8,077 | 7,881 |
| Other revenue | 6,061 | 3,788 |
| Total operating revenues | 149,917 | 144,220 |
| Operating expenses: | | |
| Personal services | 47,671 | 50,523 |
| Materials and supplies | 6,470 | 8,055 |
| General and administrative | 12,154 | 26,995 |
| Environmental clean-up | 22,783 | - |
| Other operating expenses | 62,967 | 63,833 |
| Total operating expenses | 152,045 | 149,406 |
| Operating loss | (2,128) | (5,186) |
| Nonoperating revenues (expenses) | 5,137 | (2,981) |
| Special item - sale of property | 126,014 | 0 |
| Change in net assets | 129,023 | (8,167) |
| Net assets at beginning of year | 324,794 | 319,019 |
| Prior period adjustment | 0 | 13,942 |
| Net assets at end of year | 453,817 | 324,794 |

Clean Water Facts

- Maintains 3 treatment plants:
 - Oceanside
 - Dry weather capacity: 23 MGD
 - Wet weather capacity: 65 MGD
 - Southeast
 - Dry weather capacity: 85 MGD
 - Wet weather capacity: 250 MGD
 - North Point
 - Capacity: 150 MGD
- Maintains 2 community facilities:
 - Southeast
 - Community Center
 - Earl P. Mills Facility

Current Year Clean Water Facts

- Processed ~ 2 billion gallons of sanitary & storm runoff (Oceanside)
- Processed 23.3 billion gallons of sanitary & storm runoff (Southeast)
- Processed 953 million gallons of sanitary & storm runoff (North Point)
- Responded to 8,216 customer calls
- Performed 2,571 sewer inspections

Clean Water Enterprise

The Clean Water Enterprise operates and maintains the City's water pollution control system. The system consists of a collection of sewers, transport boxes, storage boxes, pump stations, overflow structures, treatment plants and outfall centers. Its mandate is to maximize treatment and minimize sewage overflows in accordance with state regulatory compliance. It is also responsible for the quality of sewage discharged in compliance with the National Pollutant Discharge Elimination System issued by the California Regional Water Quality Control Board and U.S. Environmental Protection Agency. Safeguarding the public health and minimizing environmental impacts from sewage contamination is its primary task.

Two treatment facilities function as the primary channels for wastewater processing: Southeast and Oceanside. The North Point Wet Weather Treatment facility is used only during seasons of heavy rainfall.

FY2000-01 Highlights

- ❖ Oceanside plant received the Association of Metropolitan Sewerage Agencies (AMSA) Platinum Award for perfect compliance with discharge permit conditions for five calendar years 1996 through 2000.
- ❖ Southeast plant received AMSA Silver Award for excellent compliance with discharge permit conditions for calendar year 2000.
- ❖ Participated in California's ISO Demand Reduction Program curtailing electrical use during peak periods by shutting down treatment operations, and earned approximately \$1.9 million from this effort.
- ❖ Completed Heating, Ventilation and Air Conditioning (HVAC) Retrofit and upgrade project at the Southeast Community Center, which enhanced its usefulness to the Bayview/Hunter's Point community.



Financial Analysis

Net assets increased by \$10.3 million or 1.1% mainly due to an increase in restricted net assets as a result of the receipt of loan proceeds from the State of California. These proceeds will be used to fund capital improvements.

Operating revenues decreased by \$3.7 million due to a decrease in billings to special districts of \$1.2 million from the prior fiscal year. The special districts represent selected cities outside of San Francisco County. In addition, the amount of revenue earned but unbilled at June 30, 2001 decreased by \$1.7 million from the prior fiscal year, due to a change in the estimation methodology.

Operating expenses increased by \$2.6 million or 2.2% primarily due to costs associated with increased personal services and materials and supplies necessary in fiscal 2001 due to drier weather conditions.

During fiscal year 2000, the Clean Water Enterprise received \$8.2 million in an insurance settlement from contractors. Certain property within the City was eroded due to the overflow of a local sewer, which resulted in significant damage to local properties. The City defended itself in litigation with local residents and was awarded an insurance settlement from the contractors responsible for the construction performed on the damaged sewer.

These results are based on the enterprise's audited financial statements.

Summary of Financial Operations (000s)

Comparative Net Assets

| | 2001 | 2000 |
|--|------------------|------------------|
| Current and other assets | \$271,658 | \$255,894 |
| Capital assets, net | 1,367,044 | 1,379,755 |
| Total assets | 1,638,702 | 1,635,649 |
| Current liabilities | 54,288 | 50,417 |
| Long-term liabilities | 619,693 | 630,836 |
| Total liabilities | 673,981 | 681,253 |
| Net Assets: | | |
| Invested in capital assets, net related debt | 758,884 | 765,404 |
| Restricted | 184,924 | 161,391 |
| Unrestricted | 20,913 | 27,601 |
| Total net assets | 964,721 | 954,396 |

Changes in Net Assets

| | | |
|-------------------------------------|----------------|----------------|
| Operating revenues: | | |
| Charges for services | \$ 136,821 | \$ 140,878 |
| Other operating revenues | 4,949 | 4,617 |
| Total operating revenues | 141,770 | 145,495 |
| Operating expenses: | | |
| Personal services | 34,439 | 30,020 |
| Materials and supplies | 7,140 | 6,013 |
| General and administrative | 10,020 | 9,903 |
| Other operating expenses | 66,241 | 69,337 |
| Total operating expenses | 117,840 | 115,273 |
| Operating income | 23,930 | 30,222 |
| Nonoperating expenses, net | (13,605) | (22,218) |
| Special item - insurance settlement | - | 8,176 |
| Change in net assets | 10,325 | 8,004 |
| Net assets at beginning of year | 954,396 | 938,216 |
| Net assets at end of year | 964,721 | 954,396 |

FY2000-01 Highlights

- Bureau of Finance expanded the Commercial Paper program to \$250 million to fund the Capital Budget for Water Enterprise
- The UEB completed detail design on the demolition, construction and upgrade of the Central Pump Station and its associated equipment and pipelines. This is the first in a series of seismic and general upgrades to City pump stations
- The ITS bureau developed and implemented electronic interfaces between the various SFPUC computerized systems and the City's Accounting and Materials Management System.
- WQB completed pilot testing for emergency treatment of Hetch Hetchy water

SFPUC Bureaus

Ten bureaus, with employees totaling 626, provide technical and administrative support to the operating divisions and ultimately, to the customers. They are:

- ❖ General Manager Office
- ❖ Bureau of Finance
- ❖ Utilities Engineering Bureau (UEB)
- ❖ Bureau of Information Technology Systems (ITS)
- ❖ Bureau of Personnel & Training (BPT)
- ❖ Water Quality Bureau (WQB)
- ❖ Customer Service Bureau (CSB)
- ❖ Commercial Land Management Bureau (CLMB)
- ❖ Bureau of Planning
- ❖ Bureau of Environmental Regulation & Management (BERM)

As the SFPUC is comprised of three enterprises, all expenses associated with services provided by the bureaus are allocated to the enterprises at the end of each fiscal year based on the 1998 Cost Allocation Plan, which is updated annually for budgeted expense estimates.





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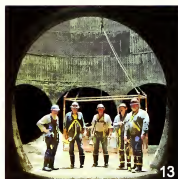
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FY2000-01 Highlights continued

- CSB introduced SFPUC Billpay Online, which allows customers to use the internet to receive, view, and pay their water and sewer bills.
- CLMB completed the sale of Bernal property in Alameda County for approximately \$126 million.
- CLMB completed negotiation of lease with Mission Valley Rock, which will result in revenues of approximately \$60 million over the life of the lease.
- Bureau of Planning initiated the development of a ten-year capital improvement program for water and clean water systems.
- Bureau of Planning developed and adopted Interim Water Shortage Allocation Plan to establish allocation method during drought between retail and wholesale customers collectively.

SFPUC staff at work:

1. Operating treatment plants
2. Repairing power lines
3. Controlling schedules
4. Conducting landscape audits
5. Reading water meters
6. Flushing water mains
7. Repairing sewer
8. Managing operations
9. Monitoring costs
10. Testing drinking water
11. Fighting fires
12. Training staff

13. Inspecting tunnels
14. Running computerized monitoring system
15. Testing crab for pollution
16. Repairing equipment



On the cover:

Photo by Therese Madden, SFPUC

Back Cover

Photo of the Pugas Water Temple by Toni Battle, SFPUC

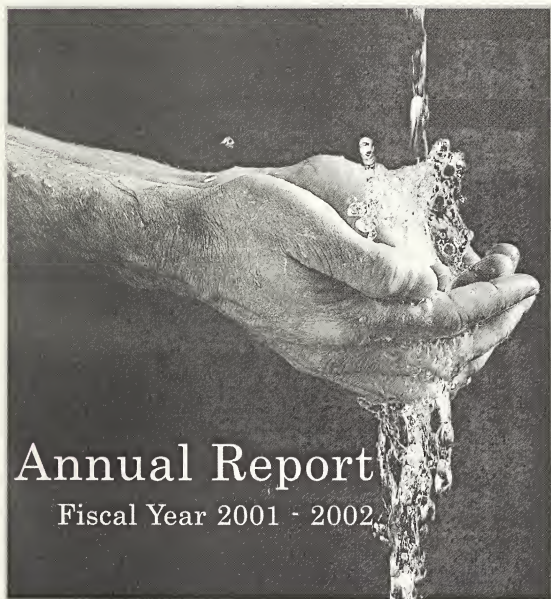
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Hetch Hetchy Water and Power Enterprise

San Francisco Water Enterprise

Clean Water Enterprise



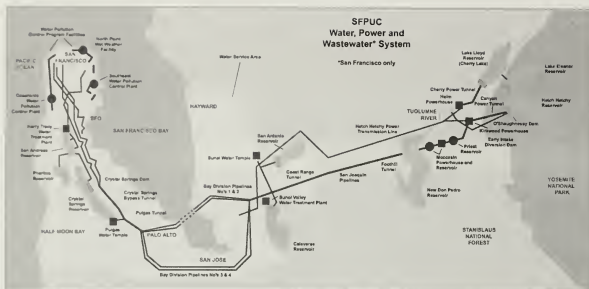


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Willie L. Brown, Jr., Mayor
City & County of San Francisco

San Francisco Public Utilities Commission

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Willie L. Brown, Jr.,
Mayor



SFPUC Commissioners Ashok Kumar Bhatt, E. Dennis Normandy, Ann Moller Caen, Jeffrey Chen, and Robert J. Costello.

The San Francisco Public Utilities Commission (SFPUCC) oversees three of the City and County of San Francisco's (City) municipal utilities:

- ◆ **Hetch Hetchy Water and Power**
Enterprise consists of water supply and power generation facilities in the Sierra Nevada;
- ◆ **The San Francisco Water Enterprise**
consists of a treatment and distribution system, which delivers drinking water to more than 2.4 million customers in the San Francisco Bay Area;
- ◆ **The Clean Water Enterprise**
treatment and disposal system collects and treats sewage and storm water flows within San Francisco.

Each of the three utilities represents a separate business enterprise within the SPUC, which functions as a department of the City. The Mayor of San Francisco appoints a five-member Commission, each for four-year terms to govern the SPUC. The Commission appoints the General Manager who serves as the chief administrative officer and is responsible for the SPUC's day-to-day operations. The General Manager provides overall direction and leadership, appoints senior staff to manage the three enterprises and oversees the activities of the SPUC.

A Message from....Patricia E. Martel, General Manager

After the devastating earthquake of 1906, San Francisco recognized the importance of a plentiful and reliable source of high quality water to meet its needs. Through Congressional action in 1912, the city secured rights to the Tuolumne River water supply in the high Sierra Nevada Mountains. San Francisco's current Hetch Hetchy water system was conceived, designed and built in the early years of the last century. Nearly 90 years later, thanks to innovative civic vision and engineering mastery, the system continues to serve customer water needs in a Bay Area whose growth and prosperity were unimaginable at the time it was built.

The San Francisco Public Utilities Commission (SFPUC) manages this great resource to ensure the health and well-being of our customers, and support an economy dependent on high quality water for its tourism, manufacturing, and biotechnology industries. Looking to the future, the SFPUC plans to rebuild the Hetch Hetchy water system in cooperation with the people of San Francisco and our regional water customers to secure adequate, reliable water deliveries for the next 100 years.

- **Securing Adequate Water Supplies**

With the continuing prosperity in the Bay Area, water needs have grown over the past century. There are insufficient water supplies in dry years to meet all needs, so effective drought planning is critical. In 2002, the SFPUC negotiated a water supply allocation plan with its wholesale customers to equitably distribute scarce water supplies in dry years. Reliability improvements to Sutro and College Hill Reservoirs in San Francisco strengthened our ability to maintain storage of critical water supplies during a major seismic event.

- **Strengthening the Water Delivery System**

In fiscal year 2002 the SFPUC issued \$140 million in 1997 Proposition A and B water revenue bonds to strengthen water delivery pipelines, upgrade pump stations and reservoirs, and improve water disinfection and treatment. To provide delivery flexibility during seismic events, the SFPUC built the new Clarendon Pump Station, which enhanced the system's operations to move water supplies efficiently around the city's hills. To ensure future water delivery reliability, a long-range \$3.6 billion plan was developed to rebuild the Hetch Hetchy water system over the next decade.

- **Ensuring Water Quality**

The SFPUC has made a major investment in upgrading its two water treatment plants in the Sunol Valley and San Mateo County to meet new water quality regulations. Construction at both plants will be complete in 2003-04, providing increased treatment capacity and improved efficiency. In San Francisco, the SFPUC is retrofitting the water circulation and treatment systems in city storage reservoirs to assure the best possible quality at your tap. The conversion to chloramine disinfection is on schedule for 2003-04, to provide longer lasting protection against bacteria and viruses in treated water.



*Patricia E. Martel
General Manager*



*Construction worker at
College Hill Reservoir.*



*Sunol Valley Water
Treatment Plant.*

- **Pursuing Energy Reliability**

Energy reliability remained a significant issue in fiscal year 2002. The SFPUC hosted a citywide Sustainability Fair to highlight energy conservation and renewable resources. City traffic lights were replaced with new energy-saving bulbs that enhanced visibility and reduced energy use by 82%. The SFPUC took aggressive action to reduce the city's risks and liabilities, inherent to the volatile power wholesale market, and diversify our portfolio of energy resources.

- **Protecting the Bay and Ocean**

For more than 60 years, the SFPUC combined sewer system has protected San Francisco Bay and the Pacific Ocean by capturing rainfall and street runoff, and sending it for treatment to the city's two water pollution control plants before discharge. In fiscal year 2002 the SFPUC announced plans to initiate a Clean Water Master Planning Process to seek innovative solutions that address water pollution control, expanded reclamation, decentralized wastewater treatment facilities, environmentally sound pollution control measures, as well as long-standing environmental justice issues.

- **Staying Safe**

Post- September 11th responses in fiscal year 2002 posed a challenge to the SFPUC as attention was focused on the nationwide threat of terrorism by increasing security staffing, installing additional security deterrents and improving surveillance to protect facilities, operations, watersheds and personnel.

- **Looking Forward**

Looking forward to the challenging tasks ahead will occupy most of the SFPUC's time, resources and attention in the near future, as the organization begins to implement rebuilding the Hetch Hetchy water system, upgrading our water pollution control facilities and meeting future energy needs. The SFPUC will work together with San Francisco's diverse stakeholders and our regional customers to develop solutions to the problems of future reliability and ensure the high quality of life and health enjoyed by San Francisco and the Bay Area.

Patricia E. Martel
General Manager



New energy efficient lights.



Bay Division Pipelines.



Solar panels slated for Moscone Convention Center.

Hetch Hetchy Facts

- ◆ 660,000 acre feet of water storage facilities
- ◆ 570,000 acre feet of storage in New Don Pedro Reservoir
- ◆ 4 hydroelectric generation stations with combined maximum capacity of 405 megawatts
- ◆ 650 square miles of forested watershed
- ◆ 165 miles of aqueducts, pipelines, high-voltage transmission systems, and rights-of-way
- ◆ Supplies average of 220 million gallons of water per day (MGD)
- ◆ 85% of San Francisco's drinking water supply
- ◆ 15% of San Francisco's electrical supply

Current Year

Hetch Hetchy Facts

- ◆ 31 inches of precipitation
- ◆ 450,000 acre-feet snowmelt inflow at Hetch Hetchy Reservoir from April to July - 83% of historic average
- ◆ 251,000 acre-feet spring runoff at Lakes Lloyd and Eleanor from April to July - 81% of historic average
- ◆ 1.7 million MW hours total generation

Hetch Hetchy Water and Power Enterprise

Hetch Hetchy Water and Power (Hetch Hetchy) is a water and power enterprise, which provides reliable water and electricity to its customers while safeguarding the resources and assets entrusted to its care. Under pre-1914 water rights, Hetch Hetchy collects water in several reservoirs on State and Federal lands pursuant to rights-of-way granted to the City through federal legislation in 1913 (the Raker Act). The purity of Hetch Hetchy water makes filtering unnecessary. The Raker Act required Hetch Hetchy to develop power generation in order to maximize the beneficial use of the water.

Hydroelectric power from Hetch Hetchy provides electricity to City facilities (e.g., City Hall, Municipal Railway, Moscone Center, Port, Airport, Recreation and Park, City hospitals, City street lighting, water and sewer utilities, etc.). Power is also sold to a limited number of retail customers in San Francisco and other public agencies and municipalities on a wholesale basis. Hetch Hetchy's wholesale power customers include the Modesto and Turlock Irrigation Districts, which have priority rights under the Raker Act.

Fiscal Year 2001-02 Highlights

- ❖ Water and Power Operations - Optimized power distribution on projects such as Laguna Honda Hospital, Asian Art Museum, and Third Street corridor, resulting in lower wheeling charges; improved field services to customers in need of high voltage maintenance; improved Hetch Hetchy load forecasting and power generation scheduling to optimize production; assessed new methods to monitor power market prices and analyze price volatility.
- ❖ Electric Utility Regulatory Analysis and Advocacy - Protected Hetch Hetchy power rights, reviewed and commented on power market design proposals, California Independent System Operator (CAISO) regulatory activities; analyzed the impact of PG&E's bankruptcy; monitored and responded to California Public Utilities Commission (CPUC) and Federal Energy Regulatory Commission (FERC) ratemaking issues.
- ❖ Diversifying Energy Resources - Developed the City's Electricity Resource Plan; implemented renewable energy and energy efficiency programs; installed photovoltaic solar energy and energy efficiency measures at the Moscone Convention Center Project; completed the installation of a digester gas cogeneration plant at the Southeast Water Pollution Control Plant to recycle methane gas into heat and electricity; developing alternative power resources to replace Hunters' Point power plant; implemented energy efficiency measures in City agencies such as San Francisco General Hospital and Housing Authority; and investigated research and development projects for renewable and distributed energy.

Financial Analysis

Net assets increased by \$15.5 million or 6% in fiscal year 2002, mainly due to a reduction in funds transferred to the General Fund of the City.

Operating revenues increased by \$4.8 million or 4% to \$125.8 million, primarily due to the increase in charges for services of \$4.7 million resulting from the increase in sales of power and related services. Non-operating revenues decreased by \$266 thousand or 6% due to a decrease in interest and investment income of \$2.2 million and an increase of \$1.9 million in other non-operating revenues, including FEMA reimbursements for costs incurred to repair damage associated with certain natural disasters.

Operating expenses increased by \$6.8 million or 6% to \$113.8 million, primarily due to the increase in power costs of \$10.4 million, offset by a reduction in general and administrative expenses of \$3.0 million.

Capital contributions represent the transfer of assets to Hetch Hetchy from the San Francisco International Airport (SFIA) as a result of the phased completion of a power substation located on SFIA property. The amount reported as of June 30, 2001 reflects the final transfer of assets due to project completion.

Transfers to the City represent amounts provided to the City to finance the General Fund. Transfers were reduced to only \$382 thousand compared with \$29.9 million in 2001, as Hetch Hetchy needed to preserve available funds for power purchases in a volatile market environment.

These results are based on the enterprise's audited financial statements.

Summary of Financial Operations (000's)

Comparative Net Assets

| | 2002 | 2001 |
|--|-------------------------|-------------------------|
| Current and other assets | \$70,354 | \$59,124 |
| Capital assets, net | <u>208,658</u> | <u>205,071</u> |
| Total assets | 279,012 | 264,195 |
| Current liabilities | 12,196 | 12,023 |
| Long-term liabilities | <u>5,490</u> | <u>6,372</u> |
| Total liabilities | 17,686 | 18,395 |
| Net assets: | | |
| Invested in capital assets, net related debt | 208,658 | 205,071 |
| Unrestricted | <u>52,668</u> | <u>40,729</u> |
| Total net assets | <u>\$261,326</u> | <u>\$245,800</u> |

Comparative Changes in Net Assets

| | | |
|----------------------------------|-------------------------|-------------------------|
| Operating revenues: | | |
| Charges for services | \$125,573 | \$ 120,863 |
| Rental income | <u>204</u> | <u>137</u> |
| Total operating revenues | 125,777 | 121,000 |
| Operating expenses: | | |
| Personal services | 16,647 | 14,243 |
| Materials and supplies | 1,586 | 1,293 |
| Purchased power | 54,261 | 44,237 |
| Transmission costs | 11,076 | 10,666 |
| General and administrative | 8,677 | 11,711 |
| Other operating expenses | <u>21,507</u> | <u>24,850</u> |
| Total operating expenses | 113,754 | 107,000 |
| Operating income | 12,023 | 14,000 |
| Non-operating revenues, net | 3,885 | 4,151 |
| Capital contributions | 0 | 270 |
| Transfers to the City | <u>(382)</u> | <u>(29,850)</u> |
| Change in net assets | 15,526 | (11,429) |
| Net assets at beginning of year | <u>245,800</u> | <u>257,229</u> |
| Net assets at end of year | <u>\$261,326</u> | <u>\$245,800</u> |

Water Facts

Regional Water

- ◆ 40,000 acre watershed in Alameda County
- ◆ 23,000 acre watershed on the Peninsula
- ◆ Harry Tracy Treatment Plant: 144 MGD
- ◆ Sunol Treatment Plant: 118 MGD
- ◆ Provides 15% of water supply from Alameda and Peninsula watersheds

Local Water

- ◆ 20 pump stations
- ◆ 15 reservoirs with storage of nearly 400 million gallons
- ◆ 13 disinfection stations
- ◆ 9 water storage tanks
- ◆ 8 water pressure reducing stations
- ◆ 1,250 miles of water mains within San Francisco, Yerba Buena Island, Treasure Island and Hunter's Point

Current Year Facts

- ◆ Accounts serviced: 170,133
- ◆ Consumption: 249.4 MGD (including 29 suburban water agencies)

Water Supply & Treatment

- ◆ Harry Tracy Treatment Plant average: 45 MGD
- ◆ Sunol Treatment Plant average: 29 MGD

City Distribution Division

- ◆ Responded to 5+ two (or greater) alarm fires
- ◆ 124 water main connections
- ◆ 641 new service installations
- ◆ 122 water main break repairs
- ◆ 5,228 meter repairs/replacements

San Francisco Water Enterprise

The Water Enterprise consists of two divisions: the Water Supply & Treatment Division and the City Distribution Division.

Water Supply and Treatment Division (WST) is responsible for the water supplies from Hetch Hetchy and local reservoirs to 1.6 million customers in Alameda, Santa Clara and San Mateo counties, and 800,000 in the City and County of San Francisco. Its mission is to operate as an effective, reliable regional water supplier, while managing resources in an environmentally sound manner.

City Distribution Division (CDD) is responsible for the transmission, storage and delivery of water to San Francisco's residential and commercial customers. CDD also provides a range of services, which include 24 hour-a-day on-call emergency response. The division maintains, repairs and upgrades water mains; provides assistance to customers' water concerns (i.e., underground leak detection and repair); and oversees work performed by outside utilities, developers and contractors. It provides landscape maintenance for 984 acres of division lands, including rights-of-way, reservoirs, open space and parks.

Fiscal Year 2001-02 Highlights

Water Supply & Treatment

- ◆ Maintained 260 vehicles and 92 pieces of heavy equipment for the Regional Water program and 82 vehicles for Hetch Hetchy and PUC bureaus.
- ◆ Adopted Peninsula Watershed Management Plan.
- ◆ Initiated a Habitat Conservation Plan for Alameda watershed lands.
- ◆ Expanded fire management activities to provide additional hazardous fuel reduction programs, fire pre-suppression improvements, emergency staging sites and expanded fire training.
- ◆ Installed throttles on Bay Division pipelines at Pulgas Valve Lot to provide for future remote operations.

City Distribution Division

- ◆ Designed 13 water main and feeder replacement projects.
- ◆ Completed Sutro Reservoir Erosion Control project.
- ◆ Retrofitted College Hill Reservoir (built in 1870) and returned it to service.
- ◆ Implemented technology and equipment for precision alignment of pumps and motors to reduce maintenance costs.
- ◆ Utilized goats for weed abatement at Summit and College Hill Reservoirs.

Financial Analysis

Net assets decreased by \$1.7 million, mainly due to an operating loss of \$1.2 million. In 2001, there was a one-time gain of \$126 million on the sale of 500 acres of land in Alameda County, which was used during FY2002 to fund several capital projects. As a result, unrestricted net assets decreased significantly from 2001.

Operating revenues decreased by \$2.7 million or 2% to \$147.2 million, primarily due to a decrease in specialized services performed during the fiscal year, which resulted in a decrease of \$2.3 million or 38%. Non-operating revenue also deteriorated, including a reduction of interest income of \$2.5 million, due to a decline in interest rates on average from 6% to 4% and a reduction in other non-operating revenue of \$1.1 million.

Operating expenses decreased by \$3.6 million or 2% to \$148.4 million, primarily as a result of increases in personal services, general and administrative, and other operating expenses of \$18.3 million, offset by a decrease in expenses related to the environmental clean up of \$22.7 million to zero in fiscal 2002. The escalation in non-operating expenses can be attributed to an increase in interest expense of \$4.1 million, as a result of the increase in outstanding long-term debt. During fiscal year 2002, the Water Enterprise issued additional long-term bonds in the amount of \$140 million.

The results are based on the enterprise's audited financial statements.

Summary of Financial Operations (000's)

Comparative Net Assets

| | 2002 | 2001 |
|--|------------------|------------------|
| Current and other assets | \$378,574 | \$301,159 |
| Capital assets, net | <u>624,495</u> | <u>529,887</u> |
| Total assets | 1,003,069 | 831,046 |
| Current liabilities | 170,227 | 120,276 |
| Long-term liabilities | <u>380,738</u> | <u>256,953</u> |
| Total liabilities | 550,965 | 377,229 |
| Net Assets: | | |
| Invested in capital assets, net related debt | 244,416 | 237,035 |
| Restricted | 30,639 | 26,750 |
| Unrestricted | <u>177,049</u> | <u>190,032</u> |
| Total net assets | \$452,104 | \$453,817 |

Comparative Changes in Net Assets

| | | |
|-----------------------------------|------------------|------------------|
| Operating revenues: | | |
| Charges for services | \$135,139 | \$135,779 |
| Rents and concessions | 8,303 | 8,077 |
| Other operating revenue | <u>3,774</u> | <u>6,061</u> |
| Total operating revenues | \$147,216 | \$149,917 |
| Operating expenses: | | |
| Personal services | 49,676 | 47,671 |
| Materials and supplies | 5,955 | 6,470 |
| General and administrative | 21,003 | 12,154 |
| Environmental clean-up | 0 | 22,783 |
| Other operating expenses | <u>71,796</u> | <u>62,967</u> |
| Total operating expenses | 148,430 | 152,045 |
| Operating loss | (1,214) | (2,128) |
| Non-operating revenues (expenses) | (499) | 5,137 |
| Special item - sale of property | <u>0</u> | <u>126,014</u> |
| Change in net assets | (1,713) | 129,023 |
| Net assets at beginning of year | <u>453,817</u> | <u>324,794</u> |
| Net assets at end of year | \$452,104 | \$453,817 |

Clean Water Facts

- ◆ Operates and maintains two treatment plants and one wet weather facility:
 - Oceanside Plant**
 - ◆ Dry weather capacity: 45 MGD
 - ◆ Wet weather capacity: 65 MGD
 - Southeast Plant**
 - ◆ Dry weather capacity: 110 MGD
 - ◆ Wet weather capacity: 250 MGD
 - North Point Wet Weather Facility**
 - ◆ Capacity: 150 MGD
- ◆ Operates and maintains 900 miles of sewer pipes and collection and storage structures.
- ◆ Maintains two community facilities:
 - ◆ Southeast Community Center
 - ◆ Earl P. Mills Facility

Current Year Facts

- ◆ Processed 6.8 billion gallons of sanitary & storm water runoff (Oceanside)
- ◆ Processed 24.2 billion gallons of sanitary & storm water runoff (Southeast)
- ◆ Processed 1.08 billion gallons of sanitary & storm water runoff (North Point)
- ◆ Processed 960 million gallons of storm water runoff (Southwest Ocean Outfall)
- ◆ Responded to 9,182 customer calls
- ◆ Performed 2,742 sewer inspections

Clean Water Enterprise

The Clean Water Enterprise operates and maintains the City's water pollution control system, which provides three main functions: sewage collection, treatment, and disposal. The sewer system, which collects both sanitary and storm water flows, consists of sewers, transport and storage boxes, pump stations, overflow structures, treatment plants and outfalls. Flows from the western side of the City are treated at the Oceanside Water Pollution Control (WPC) Plant and the remainder at the Southeast WPC Plant. Under the City's Cooperative Agreement with the US Navy, Water Pollution Control Division (WPCD) operates the Treasure Island Wastewater Treatment Plant.

The majority of cities and urban areas throughout the country are currently struggling with the need to control and treat storm water flows. San Francisco has the significant advantage because the Clean Water Enterprise constructed an infrastructure that treats combined storm water and sanitary flows, resulting in improved public health and safety, and protection of the environment at a considerable financial savings.

The quality of the sewage discharged to the receiving waters is an important aspect of the Clean Water Enterprise performance. The environmental quality is monitored and the results are reported to the California Regional Water Quality Control Board, in compliance with the National Pollutant Discharge Elimination System permits.

The Clean Water Enterprise also enforces the Industrial Waste Ordinance, which further protects the receiving waters by controlling the strength and types of waste that are poured into the sewers. The effort coordinates public education programs, monitors waste streams, targets specific pollutant-generating industries, and initiates legal action against non-compliant dischargers.

The Clean Water Enterprise operates the Southeast Community Facility and the Earl P. Mills Facility, which provide valuable training and community resources to the respective neighborhoods.

Fiscal Year 2001-02 Highlights

- ❖ Decreased spending for all Operations and Maintenance expenses except power for the fourth fiscal year in a row.
- ❖ Improved odor control facilities and procedures.
- ❖ Reviewed operating procedures, completed site surveys, and tightened security effectiveness in the aftermath of the September 11th attacks.
- ❖ Operated and maintained the Treasure Island Treatment Plant and collection system.
- ❖ Assisted with dewatering operations at Candlestick Park.
- ❖ Initiated the Southeast Water Pollution Control Plant Interim Gravity Belt Thickener Facility project, to upgrade existing equipment and significantly reduce odors. Design completed, contract being bid and processed. Engineer's estimate is \$5 million.
- ❖ Upgraded the Booster Pump Station, to increase the capacity and reliability of the Southeast Treatment Plant effluent pump station by replacing pumps and drives, adding a standby pump, and updating the pump station control room. Construction started February 2000 and was completed November 2001. Total construction cost was \$10 million.

Financial Analysis

Net assets decreased by \$14.3 million or 1%, mainly due to a decrease in restricted assets as a result of loan proceeds received in prior years from the State of California used to defease certain outstanding bonds in December 2001.

Operating revenues decreased by \$7.2 million or 5% and is primarily due to a decrease in charges for services of \$6.9 million. As service revenue is a function of the Water Enterprise service volume, the decrease in charges for services can be attributable to the decrease in water consumption by City residents of approximately 2.4 million gallons per day.

Non-operating revenue decreased by \$6.4 million as a result of the decrease in interest and investment income of \$7.2 million due to lower cash balances and lower interest rates during the fiscal year.

Operating expenses increased by \$11.1 million or 9% primarily due to an escalation in costs associated with general and administrative expenses of \$8.6 million. This is attributable to increased allocated overhead expenses of approximately \$5 million and to additions to the estimated damage and claims liability of approximately \$3.6 million. The increase in overhead is the result of two factors: a general increase in allocable costs of the SFPUC of approximately \$9,800, of which the Clean Water Enterprise receives approximately 35%, and to a change in methodology and update to rates used to allocate those overhead costs. Additions to the damage and claims liability results from an unfavorable court determination in a preliminary hearing over a rate dispute between the Clean Water Enterprise and one of its customers.

These results are based on the enterprise's audited financial statements.

Summary of Financial Operations (000's)

Comparative Net Assets

| | 2002 | 2001 |
|---|------------------|------------------|
| Current and other assets | \$213,445 | \$271,658 |
| Capital assets, net | <u>1,350,385</u> | <u>1,367,044</u> |
| Total assets | 1,563,830 | 1,638,702 |
| Current liabilities | 55,612 | 54,288 |
| Long-term liabilities | <u>557,838</u> | <u>619,693</u> |
| Total liabilities | 613,450 | 673,981 |
| Net Assets: | | |
| Invested in capital assets, net related debt | 774,794 | 758,884 |
| Restricted | 108,572 | 109,993 |
| Unrestricted | <u>67,014</u> | <u>95,844</u> |
| Total net assets | \$950,380 | \$964,721 |

Comparative Changes in Net Assets

| | | |
|----------------------------------|------------------|------------------|
| Operating revenues: | | |
| Charges for services | \$129,925 | \$136,821 |
| Other operating revenues | <u>4,670</u> | <u>4,949</u> |
| Total operating revenues | 134,595 | 141,770 |
| Operating expenses: | | |
| Personal services | 34,439 | |
| Materials and supplies | 7,853 | 7,140 |
| General and administrative | 18,585 | 10,020 |
| Other operating expenses | <u>66,922</u> | <u>66,241</u> |
| Total operating expenses | 128,948 | 117,840 |
| Operating income | 5,647 | 23,930 |
| Non-operating expenses, net | (19,988) | (13,605) |
| Change in net assets, net | <u>(14,341)</u> | <u>10,325</u> |
| Net assets at beginning of year | <u>964,721</u> | <u>954,396</u> |
| Net assets at end of year | \$950,380 | \$964,721 |

FY 2001-02 Highlights

- ◆ FS issued \$140 million in 1997 Series A and B water revenue bonds to finance projects including strengthening the City's pipelines and water mains, upgrading reservoirs and pump stations, and upgrading facilities and methods used to treat and disinfect drinking water. FS also implemented an Owner Controlled Insurance Program (OCIP) wherein SFPUC will purchase insurance for contractors and subcontractors for capital projects resulting in improved insurance coverage, cost savings and greater contractor participation.
- ◆ UEB completed construction of upgrades to College Hill Reservoir, which was built in 1870. UEB completed design for upgrades to the University Mound South Reservoir, and the design for demolition and reconstruction of the Lombard Street Reservoir, which was built in 1860.
- ◆ ITS completed a pilot project for the implementation of an Electronic Document Management system (EDM). EDM will provide the SFPUC with a central depository of engineering drawings and other vital documents. The system allows for easy retrieval of these documents and will streamline and automate existing paper intensive manual processes.
- ◆ HRS underwent a major re-organization to streamline the hiring process and shorten the time it takes to fill positions. HRS also implemented the Supervisor's Academy - a 16-week training course in the essentials of supervision.

SFPUC Bureaus

The SFPUC bureaus, which employ over 600 staff members, provide technical and administrative support to the operating divisions and ultimately, to the customers. They are:

- ❖ Office of the General Manager (GM) - The GM is responsible for the management of the three enterprises (Hetch Hetchy, Water and Clean Water) and nine bureaus that comprise the SFPUC.
- ❖ Financial Services (FS) - FS is responsible for accounting, operating and capital budgeting, procurement, rate administration, debt financing, owner-controller insurance program, and risk management.
- ❖ Utilities Engineering Bureau (UEB) - UEB is responsible for the implementation of the Capital Improvement Program including design and construction management of all SFPUC facilities including dams, reservoirs and power lines from Hetch Hetchy, to water pipelines throughout the Bay Area, to the water and sewer lines within the City of San Francisco.
- ❖ Information Technology Services (ITS) - ITS is responsible for supporting business applications (i.e. water and sewer billing, maintenance management system, etc.) and the desktop network of over 1,100 personal computers.
- ❖ Human Resource Services (HRS) - HRS is responsible for labor and employee relations, staff development and training, EEO programs, outreach and recruitment, position processing and payroll.
- ❖ Water Quality Bureau (WQB) - WQB is responsible for ensuring the SFPUC complies with all water quality regulations and customer expectations through sampling and laboratory analyses, process engineering, applied research, inspections, and support to treatment plant operations for the Water and Clean Water Enterprises.

SFPUC Bureaus continued

- ❖ Customer Service (CS) - CS is responsible for billing and collection of water, sewer and retail electrical service charges, administration of customer accounts (i.e., sewer service charge appeals, high bill allowances), installation of new services, meter reading and field services, and conservation programs.
- ❖ Real Estate Services (RES) - RES is responsible for negotiating and managing leases and use permits, and to develop commercially valuable uses for SFPUC properties consistent with its utility needs.
- ❖ Bureau of Planning (Planning) - Planning is responsible for planning the development of the Capital Improvement Program, strategic and long-range planning for the Clean Water, Hetch Hetchy and Water Enterprises, and development of a legislative strategy for SFPUC interests.
- ❖ Bureau of Environmental Regulation & Management (BERM) - BERM is responsible for regulating industrial waste discharges from the sewer system, developing and implementing water pollution prevention programs, providing environmental and regulatory compliance services, and managing SFPUC's Health and Safety Program.

All expenses associated with services provided by the bureaus are allocated to the appropriate enterprise(s) at the end of each fiscal year based on the 1998 Cost Allocation Plan, which is updated annually for budgeted expense estimates.

FY2001-02 Highlights continued

- ◆ WQB developed initial emergency response plans and started working with external organizations to develop more detailed plans for response to contamination events or suspected contamination incidents. WQB also initiated a lead-free faucet giveaway program for San Francisco residents.
- ◆ CS increased the number of customers paying their water bills electronically from 8,000 to over 22,000. It has upgraded its telephone system with automated call distribution and call management system software for better management of customer contacts. CSB also upgraded its meter reading system, which includes state-of-the-art software and the latest generation of hand-held microprocessors.
- ◆ Planning updated a long-term capital improvement program for the Water Enterprise. Planning also developed a drought contingency plan for retail customers.
- ◆ BERM conducted OSHA Construction Safety Training for all construction inspectors, resident engineers and project managers, to prepare for large-scale construction projects. BERM also implemented an employee safety newsletter to communicate safety information to all employees.



Photo of Tirolunne Meadows by Matt Gass. SFPUC

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